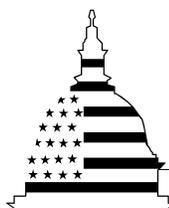


May 2006

DEPARTMENT OF
ENERGY, OFFICE OF
WORKER ADVOCACY

Deficient Controls Led
to Millions of Dollars
in Improper and
Questionable
Payments to
Contractors



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Accountability * Integrity * Reliability



Highlights of [GAO-06-547](#), a report to congressional requesters

DEPARTMENT OF ENERGY, OFFICE OF WORKER ADVOCACY

Deficient Controls Led to Millions of Dollars in Improper and Questionable Payments to Contractors

Why GAO Did This Study

The Energy Employees Occupational Illness Compensation Program Act of 2000 (EEOICPA) authorized the Department of Energy (Energy) to help its former contractor employees file state workers' compensation claims for illnesses that could be linked to exposure to toxic substances during their employment. Concerned with the relatively small number of finalized cases and the overall effectiveness of the program, Congress asked GAO to review costs incurred by Energy to administer the program. Specifically, Congress asked GAO to determine whether (1) internal controls over program payments were adequately designed to provide reasonable assurance that improper payments to contractors would not be made or would be detected in the normal course of business and (2) program payments were properly supported as a valid use of government funds.

What GAO Recommends

GAO makes 16 recommendations to help Energy and SSC NOLA strengthen controls over payments to contractors and to mitigate the risks of paying improper contract costs in the future. While Energy accepted the recommendations, it took issue with several of GAO's findings, including GAO's view of its responsibility for activities carried out through an interagency agreement. SSC NOLA concurred with the recommendations GAO made to it. GAO reaffirms its findings and recommendations.

www.gao.gov/cgi-bin/getrpt?GAO-06-547.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Linda Calbom at (202) 512-9508 or calboml@gao.gov.

What GAO Found

Energy did not establish an effective control environment over payments to contractors or overall contract costs. Specifically, because Energy lacked an effective review and approval process for contractor invoices, it had no assurance that goods and services billed had actually been received. Although responsibility for review and approval of invoices on the largest contract rested with the Space and Naval Warfare Systems Center, New Orleans (SSC NOLA) through an interagency agreement, Energy did not ensure that SSC NOLA carried out proper oversight. Energy also failed to maintain accountability for equipment purchased by contractors. Further, subcontractor agreements, which represented nearly \$15 million in program charges, were not adequately assessed, nor were overall contract costs sufficiently monitored or properly reported. These fundamental control weaknesses made Energy highly vulnerable to improper payments.

GAO identified \$26.4 million in improper and questionable payments for contractor costs, including billings of employees in labor categories for which they were not qualified or that did not reflect the duties they actually performed, the inappropriate use of fully burdened labor rates for subcontracted labor, add-on charges to other direct costs and base fees that were not in accordance with contract terms, and various other direct costs that were improperly paid. Further, certain payments toward the end of the program for furniture and computer equipment may not have been an efficient use of government funds.

Summary of Improper and Questionable Payments

Type of cost	Improper	Questionable	Total
Labor			
Labor categories ^a	\$2,498,920	\$17,686,892	\$20,185,812
Fully burdened labor rates	3,661,429	569,798	\$4,231,227
Overtime charges	3,019		\$3,019
Subtotal			\$24,420,058
Other direct costs			
Add-on charges and base fees	\$655,734		\$655,734
Per diem and commuting costs ^a	12,418	\$4,704	\$17,122
First-class travel ^a	5,207	9,119	\$14,326
Other miscellaneous payments	91,431		\$91,431
Subtotal			\$778,613
Inefficient use of government funds			
Furniture		\$821,129	\$821,129
Equipment		341,790	\$341,790
Subtotal			\$1,162,919
Total	\$6,928,158	\$19,433,432	\$26,361,590

Source: GAO.

^a The amounts reported for these categories represent the gross amount paid to Energy to its contractors and therefore do not reflect any reductions or offsets that may be due the contractors for the goods and services that were provided. Any potentially recoverable amounts would need to be determined after consideration of these reductions or offsets.

These improper and questionable payments represent nearly 30 percent of the \$92 million in total program funds spent through September 30, 2005, but could be even higher given the poor control environment and the fact that GAO only reviewed selected program payments.

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Abbreviations

BPA	blanket purchase agreement
CO	contracting officer
COR	contracting officer's representative
DCAA	Defense Contract Audit Agency
DOJ	Department of Justice
DOL	Department of Labor
EEOICPA	Energy Employees Occupational Illness Compensation Program Act of 2000
ES&H	Office of Environment, Safety, and Health
FAR	<i>Federal Acquisition Regulation</i>
FSS	Federal Supply Schedule
FTR	<i>Federal Travel Regulation</i>
FTS	Federal Technology Service
GSA	General Services Administration
IRS	Internal Revenue Service
OWA	Office of Worker Advocacy
SEA	Science and Engineering Associates, Inc.
SSC NOLA	Space and Naval Warfare Systems Center, New Orleans
TDI	Technical Design, Inc.

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United States Government Accountability Office
Washington, D.C. 20548

May 31, 2006

The Honorable Charles E. Grassley
Chairman
Committee on Finance
United States Senate

The Honorable Jeff Bingaman
Ranking Minority Member
Committee on Energy and Natural Resources
United States Senate

The Honorable Jim Bunning
United States Senate

The Energy Employees Occupational Illness Compensation Program Act of 2000 (EEOICPA) was passed by Congress, in part, to provide for timely compensation of former nuclear weapons workers who sustained illnesses that could be linked to exposure to toxic substances while employed at a Department of Energy (Energy) facility.¹ Subtitle D of EEOICPA instructed Energy to assist its contractors' employees by developing and submitting state workers' compensation claim applications to an independent physician panel for review of each claimant's potential eligibility for workers' compensation benefits. Subtitle D of EEOICPA did not instruct Energy to pay the benefits due an eligible worker, but instead authorized Energy to assist the claimant in filing a claim to receive compensation from a state workers' compensation program.

Concerned with the relatively small number of finalized cases and the overall effectiveness of the program, the Senate Energy and Natural Resources Committee held three hearings from November 2003 through March 2004 that highlighted programmatic challenges to achieving the

¹Pub. L. No. 106-398, §. 1, div. C, title xxxvi, 114 Stat. 1654A-494 (Oct. 30, 2000).

program's objectives and Energy's limited progress in overcoming them.² Further, in May 2004, we issued a report identifying issues with the claims review process. For example, we reported that a shortage of qualified physicians serving on the review panels continued to constrain Energy's capacity to decide cases more quickly.³ In October 2004, EEOICPA was amended to repeal Subtitle D and add a new Subtitle E to be administered by the Secretary of Labor.⁴

Prior to the amendment of EEOICPA, in a letter dated August 30, 2004, you asked us to review costs incurred by Energy in its administration of Subtitle D by considering the design of internal controls over expenditures and the propriety of program payments. Specifically, we determined whether (1) internal controls over program payments were adequately designed to provide reasonable assurance that improper payments to contractors would not be made or would be detected in the normal course of business and (2) program payments were properly supported as a valid use of government funds.

To address these objectives, we considered payments made by the Office of Worker Advocacy (OWA), the Energy office tasked with administering Subtitle D, from the inception of the program in October 2000 through September 30, 2005.⁵ We primarily focused on payments to key contractors that received approximately 60 percent of the \$92 million in program expenditures through September 2005. We reviewed the design of controls over program payments, including payments made to contractors. We also reviewed controls designed to monitor overall contractor costs. We used a

²The hearings on Energy's administration of EEOICPA, Subtitle D, were held by the Senate Committee on Energy and Natural Resources on November 21, 2003, December 6, 2003, and March 30, 2004. GAO's testimony statements are GAO, *Energy Employees Compensation: Case-Processing Bottlenecks Delay Payment of Claims*, [GAO-04-249T](#) (Washington, D.C.: Nov. 21, 2003); *Energy Employees Compensation: Case-Processing Bottlenecks Delay Payment of Claims*, [GAO-04-298T](#) (Washington, D.C.: Dec. 6, 2003); and *Energy Employees Compensation: Obstacles Remain in Processing Cases Efficiently and Ensuring a Source of Benefit Payments*, [GAO-04-571T](#) (Washington, D.C.: Mar. 30, 2004).

³GAO, *Energy Employees Compensation: Even with Needed Improvements in Case Processing, Program Structure May Result in Inconsistent Benefit Outcomes*, [GAO-04-515](#) (Washington, D.C.: May 28, 2004).

⁴Pub. L. No. 108-375, div C, title xxxi, § 3161(i), 118 Stat. 1811, 2178 (Oct. 28, 2004).

⁵After Subtitle D was repealed and the program effectively transferred to the Department of Labor (DOL), Energy continued to provide claims research activities at the field offices in support of DOL and other agency activities.

variety of forensic auditing techniques, including data mining, to identify payments for detailed review. We requested comments on a draft of this report from the Secretary of Energy and on selections of this report from the Commanding Officer of the Space and Naval Warfare Systems Center, New Orleans (SSC NOLA). We received written comments from Energy's Deputy Assistant Secretary of Planning and Administration, Office of Environment, Safety and Health and the Commanding Officer of SSC NOLA. We have incorporated the comments as appropriate. The comments are reprinted in appendixes II and III. We performed our work in accordance with generally accepted government auditing standards in Washington, D.C., and three contractor locations from February 2005 through March 2006. Further details on our scope and methodology can be found in appendix I.

Results in Brief

Energy's control environment over payments to contractors and overall contract costs was not effective in reducing the risk of improper payments. Energy did not establish fundamental control activities, such as an effective review and approval process for contractor invoices that enabled it to verify that goods and services billed for had actually been received and charged at the agreed-upon amounts. Specifically, contractor services were not adequately monitored, labor rates were not verified, and other direct costs lacked adequate supporting documentation. Through an interagency agreement, SSC NOLA was responsible for the review and approval of Science and Engineering Associates, Inc. (SEA), invoices, among other administrative duties, but did not adequately perform this function. For example, the SSC NOLA official responsible for observing services made no site visits to SEA's main performance location after February 2004, when SEA more than tripled its workforce assigned to the program, and made only periodic visits before that time. Energy, however, took no steps to assure itself that SSC NOLA was properly carrying out its responsibilities. Energy also did not have sufficient controls over equipment purchased by contractors for the program and, as a result, could not fully account for equipment during the program or at the expiration of the contracts. Additionally, Energy and its contracting partners, the General Services Administration (GSA) and SSC NOLA, did not adequately assess subcontracted activity, which represented nearly \$15 million in payments by the program. Further, Energy made errors in reporting total contract costs in its internal and external financial reports, and did not effectively monitor cumulative contract costs—an important step in managing overall contract costs, particularly for time and materials contracts.

These fundamental internal control weaknesses and Energy's poor overall control environment made Energy highly vulnerable to improper payments and contributed to \$26.4 million in improper and questionable payments to contractors that we identified through a variety of forensic auditing techniques. Of these improper and questionable payments, \$24.4 million related to labor charges. These included \$2.5 million in improper payments to certain contractors under inappropriate labor categories, including employees in labor categories for which they were not qualified or that did not reflect the duties they actually performed. Payments for labor charges further included \$17.7 million in questionable payments where, for example, the labor category descriptions provided insufficient criteria by which to assess whether the person was qualified under that labor category. In addition, Energy paid two contractors for subcontracted labor costs using fully burdened labor rates—rates that included base wages plus fringe benefits, overhead costs, and profit—for which there was no basis under the contracts. This resulted in more than \$4.2 million in improper and questionable payments by Energy. We also identified \$778,613 in improper and questionable payments for other direct costs, including amounts for add-on charges and other fees not provided for in the contracts, first-class travel, and unallowable per diem and commuting costs. We found, for instance, that Energy paid contractor charges for per diem for out-of-town personnel for weeks at a time when time records we reviewed showed that they were not working. Finally, we questioned whether more than \$1 million in payments for furniture and office equipment purchased toward the end of the program, much of which was not used by OWA, was an efficient use of government funds. These improper and questionable payments for contract costs represent nearly 30 percent of the \$92 million in total program funds spent through September 30, 2005, but could be even higher given the poor control environment and the fact that we only reviewed selected program payments.

We are making 16 recommendations to address the issues identified in this report. We are making 14 recommendations to Energy to (1) improve controls over the review and approval process for contractor invoices; (2) strengthen accountability for government-owned equipment purchased by contractors; (3) improve reporting and control of overall contract costs, including subcontractor costs; and (4) pursue opportunities for recovery of improper and questionable payments identified in this report. We are also making 2 recommendations to SSC NOLA to reassess its procedures for carrying out its responsibilities for delegated contract administration in connection with interagency agreements.

In written comments on a draft of this report, Energy stated that it agreed with the spirit and intent of our recommendations and that it will give careful consideration to each of them. However, Energy took issue with our core finding that it was responsible for its program activities carried out through the cooperation of other agencies and contractors through use of an interagency agreement. It also disagreed with some of our other findings, including those related to improper payment of certain contractor fees. In addition, Energy described some of the corrective actions it is implementing to improve its controls, including those over interagency contracting.

We continue to believe that Energy cannot assign or delegate away its responsibility for ensuring the success of contracted efforts as well as the propriety of payments under interagency agreements. Also, we stand by our assessment of the improper and questionable nature of certain fees Energy paid to its contractors. Our more detailed responses to these comments are provided in the Agency Comments and Our Evaluation section of this report and in appendix II.

SSC NOLA concurred with our recommendations and indicated that it has plans to complete actions on the recommendations by August 1, 2006.

Background

EEOICPA has two major components. The Department of Labor (DOL) administers Subtitle B, which provides eligible workers who were exposed to radiation or other toxic substances and who subsequently developed illnesses, such as cancer and lung disease, a onetime payment of up to \$150,000 and covers future medical expenses related to the illness. The benefits are payable from a compensation fund established by EEOICPA. Subtitle B is not covered in this report. Prior to October 2004, Energy administered Subtitle D to help its contractors' employees file state workers' compensation claims for illnesses determined by a panel of physicians to have been caused by exposure to toxic substances in the course of employment at an Energy facility. This report covers payments made to administer Subtitle D.

To facilitate outreach to potential claimants and to help claimants obtain work and medical records to initiate claims under EEOICPA, Energy

established 11 regional resource centers.⁶ These resource centers were a gateway for claimants applying for assistance under EEOICPA under both Subtitle D, administered by Energy, and Subtitle B, administered by DOL. Energy and DOL shared the resource centers' costs of operation, staffing, and training. To achieve this, DOL reimbursed Energy for about half of the costs of its contract with Eagle Research Group, Inc., the company that staffed and operated most of the resource centers. Additionally, DOL reimbursed Energy for a portion of other costs Energy paid directly, such as those for the leased space for the centers.

After EEOICPA claims were received through the resource centers and headquarters, Energy requested its field offices to locate records that would support the claims, such as employment, medical treatment, and toxic substance exposure records. Energy forwarded the information collected to claim developers and various assistants who assembled the information into case files. A panel of physicians reviewed the case files to determine whether exposure to a toxic substance during employment at an Energy facility was at least as likely as not to have caused, contributed to, or aggravated the claimed medical condition. In addition to the panel physicians, other doctors performed quality assurance checks of the case files before the claims were submitted to the physician panels and again after the physician panels had made recommendations. All panel determinations were finalized by a medical director employed by Energy. Energy communicated with applicants through an EEOICPA hotline and through letters.

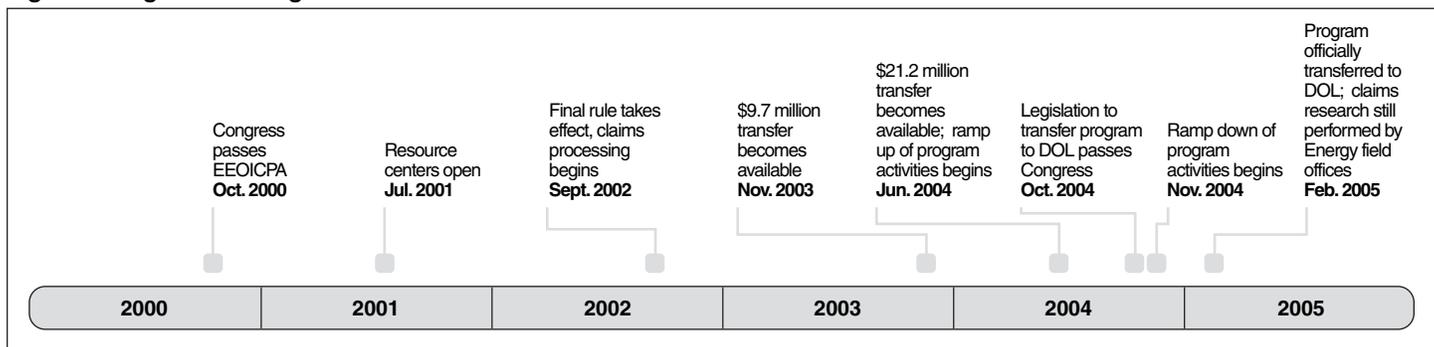
Energy began accepting applications for Subtitle D in July 2001 when the majority of the resource centers opened, and began developing cases in the fall of 2002 when its final administrative rule took effect.⁷ While Energy got off to a slow start in processing cases, completing only 6 percent of approximately 23,000 cases by December 31, 2003, Energy later increased claim development activities, which resulted in a backlog of claims awaiting review by the physician panels. In June 2004, Energy transferred

⁶The resource centers were located in Espanola, New Mexico; Richland, Washington (Hanford); Idaho Falls, Idaho; Las Vegas, Nevada; North Augusta, South Carolina (Savannah River); Oak Ridge, Tennessee; Paducah, Kentucky; Portsmouth, Ohio; Westminster, Colorado (Rocky Flats); Livermore, California; and Anchorage, Alaska.

⁷Energy published its final rule at 67 Fed. Reg. 52841 (Aug. 14, 2002), codified at 10 C.F.R. Part 852, "Guidelines for Physician Panel Determinations on Worker Requests for Assistance in Filing for State Workers' Compensation Benefits," which became effective on September 13, 2002.

\$21.2 million in funds to OWA in an effort to clear the backlog of claims. During the same time, it increased the number of case developers and physicians serving on the review panels. Legislation was also moving through Congress as early as June 2004 to transfer the administration of Subtitle D from Energy to DOL.⁸ Ultimately, in October 2004, Congress repealed Subtitle D and created Subtitle E, to be administered by DOL. In light of the potential transfer, Energy ceased hiring new case developers in August 2004, then gave official instruction to cease claims processing in November 2004. Energy received \$112.6 million in appropriated funds (including transfers) through fiscal year 2005 for its EEOICPA activities and spent over \$92 million. Energy’s field offices continue to research claims that are now processed by DOL under Subtitle E. See figure 1 for a time line of significant OWA program events.

Figure 1: Significant Program Events



Source: GAO.

Under Subtitle D of EEOICPA, Energy’s role was to assist applicants in pursuing state workers’ compensation benefits but not to pay any benefits to the applicants. Therefore, the costs associated with Energy’s EEOICPA activities are administrative costs only. We analyzed Energy’s program costs by major program activity, as shown in table 1.

⁸S. 2400, 108th Cong. (passed by the Senate on June 23, 2004).

Table 1: Total Program Costs for October 2000 through September 30, 2005

Activity	Amount	Major contractors performing these activities
Managed and operated 11 resource centers	\$11,817,528	Eagle Resource Inc. (\$10.4 million)
Researched cases and exposure records at Energy offices	29,081,346	Primarily performed by major facility operating contractors ^a
Prepared/assembled cases, including the associated furniture and office space for personnel; developed and maintained the Case Management System	34,321,660	Science and Engineering Associates, Inc. ^b (\$31.5 million)
Established physician panels to review cases, staffed the EEOICPA hotline, supported the Advisory Committee, and provided program and administrative personnel	13,611,440	Westwood Group, Inc. (\$10.3 million) Technical Design, Inc. (\$3.3 million)
Other (such as travel for federal employees and information technology management beginning in June 2004)	3,485,097	
Total program costs reported by Energy through September 30, 2005	\$92,317,071	
Major contracts GAO reviewed		\$55,500,000

Source: GAO.

^aEnergy's major facility operating contractors, in general, operated national laboratories and performed the EEOICPA case research activities. They are subject to audit by Energy's Inspector General and were not considered in our review.

^bIncludes \$28.8 million under Energy's interagency agreement with SSC NOLA and \$2.7 million under Energy's contract with SEA.

Through multiple contracts in some cases, four major contractors performed the majority of OWA's program activities.

- Eagle Research Group, Inc. (Eagle), staffed and operated the resource centers from September 2001 through February 2005 under time and materials task orders issued under a GSA Federal Supply Schedule (FSS)⁹ contract.
- Westwood Group, Inc. (Westwood), administered the physician panels, provided a quality-assurance check on claims, managed the EEOICPA hotline, and coordinated the field office research requests. Additionally, Westwood provided certain other administrative services. Energy obtained Westwood's services through two time and materials task

⁹GSA established the FSS program in 1949 to facilitate federal agencies' purchases of common products and services from commercial vendors through schedule contracts.

orders issued under a GSA FSS contract. One task order was in effect from August 2001 through February 2005. The other began in September 2004 and can be extended through September 2009 if Energy exercises the four option periods. Under the option periods and current statement of work, Westwood would continue its analytical services relating to the EEOICPA claims research and other administrative activities for Energy's Office of Environment, Safety, and Health (ES&H).

- Technical Design, Inc. (TDI), provided administrative personnel as well as analysts trained in environment and health issues. TDI provided services to OWA under three consecutive contracts issued by Energy. All three were cost reimbursement contracts that contained performance incentives. The first contract was described by Energy as a cost plus incentive fee. The second and third contracts were cost plus award fee. Westwood also provided additional services to OWA through TDI under these contracts.

In addition to services provided to OWA, both Westwood and TDI also provided other services to Energy's ES&H. On their monthly invoices, Westwood and TDI identified OWA services separately from other ES&H services.

- SEA, under its first task order, provided information technology services to create, develop, and maintain the Case Management System to track the progress of individual cases. Under subsequent task orders, services broadened over time so that SEA provided case developers and assistants who performed case processing activities.¹⁰ SEA ultimately provided services equal to approximately one-third of OWA's program costs. In January 2004, Sidarus, Inc. (Sidarus), purchased SEA. In June

¹⁰GSA's Inspector General reported that of the three SEA task orders for services provided in fiscal years 2002, 2003, and 2004, the task orders for 2003 and 2004 included case processing activities in addition to information technology activities and were therefore outside the scope of the underlying GSA FSS contract and a misuse of the contract vehicle. Further, the GSA Inspector General concluded that the statement of work for the second task order was vague and open-ended, which discouraged competition. See General Services Administration, *Audit of Federal Technology Service's Client Support Center Greater Southwest Region*, Report Number A040097/T/7/Z05011 (Washington, D.C.: Dec. 10, 2004), and Letter to Senator Charles Grassley, from GSA's Inspector General, July 2004.

2004, Sidarus was renamed Apogen Technologies, Inc.¹¹ SEA continues to do business as SEA.

SEA's services were initially obtained by Energy through a memorandum of agreement (referred to in this report as an interagency agreement) between Energy and SSC NOLA.¹² To implement the interagency agreement, SSC NOLA used GSA's Federal Technology Service (FTS) to utilize an existing blanket purchase agreement (BPA) between SEA and GSA's FTS, dated August 2000, that was entered into under a GSA FSS contract. Under the BPA, GSA's FTS issued three consecutive time and materials task orders to SEA to provide services to Energy. The interagency agreement between Energy and SSC NOLA took effect in December 2001 and was scheduled to run for 3 years. Under this arrangement, GSA paid SEA for its services and was reimbursed by SSC NOLA. SSC NOLA received reimbursement from Energy. Energy is the customer and final payer for SEA's services. SSC NOLA elected to end work under the interagency agreement on September 30, 2004. In this report, we refer to payments to SEA as payments by Energy.

In February 2004, Energy began pursuit of a new contract to replace the interagency agreement between Energy and SSC NOLA. However, the new procurement action was not completed by the end of the interagency agreement on September 30, 2004, and Energy issued a time and materials bridge contract directly with SEA beginning October 1, 2004, for a base period of 3 months to continue case development activities and, eventually, assist in terminating and transferring the program. Energy's direct contract with SEA expired in December 2004.

Table 2 provides a description of two contract types used to administer OWA: cost reimbursement and time and materials. OWA utilized two different variations of cost reimbursement contracts: cost plus incentive fee and cost plus award fee. A description, common applications, benefits and risks associated with the contract type, and constraints or requirements for the government are listed for each type.

¹¹On March 23, 2006, counsel to SEA told us that since acquiring SEA, Apogen has put a new management team in place.

¹²Energy executed an interagency agreement with SSC NOLA under the Economy Act, 31 U.S.C. § 1535.

Table 2: Descriptions of Contract Vehicles Used by Energy for the OWA Program

Contract vehicle	Description	Applications	Benefits and risks	Constraints/government requirements
Cost reimbursement: cost plus incentive fee and cost plus award fee	A contract that provides for the payment of the contractor's allowable incurred costs to the extent prescribed in the contract, not to exceed a ceiling.	Appropriate when uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use a fixed-price contract.	Benefits: Allows the government to meet complex or unique requirements.	May be used only when the contractor's accounting system is adequate for determining allowable costs under the contract and appropriate government surveillance or oversight will be provided.
Cost plus incentive fee	Cost plus incentive fee:	Cost plus incentive fee:	May encourage economic, efficient, and effective performance when a cost reimbursement contract is necessary.	Cost plus incentive fee:
\$0.9 million Contractor: TDI	Provides for an initially negotiated fee that is later adjusted by a formula.	May be used when a target cost and a fee-adjustment formula that are likely to motivate the contractor to manage effectively can be negotiated.	Risk: Shifts cost risk from the contractor to the government.	Fee adjustment formula should provide an incentive that will be effective over the full range of reasonably foreseeable variations from the contract's target cost.
Cost plus award fee \$2.4 million	Cost plus award fee:	Cost plus award fee:	Appropriate when the work does not lend itself to developing incentive targets.	Cost plus award fee:
Contractor: TDI	Provides for a fee consisting of a base amount and an award amount based upon a judgmental evaluation by the government.			Any additional administrative effort and cost required to monitor and evaluate the contractor's performance are justified by the expected benefits.
Time and materials \$52.2 million	Contract that provides for direct labor hours billed at fixed hourly rates that include wages, overhead, general and administrative expenses, and profit and contractors' materials at cost.	May be used only when it is not possible at the time of placing the contract to estimate accurately the extent or duration of the work or to anticipate costs with any reasonable degree of confidence.	Benefit: Can fulfill a special need. Risk: Does not provide a positive profit incentive for contractor to control costs.	May be used only after the contracting officer determines that no other contract type is suitable, and the contract must include a ceiling price that the contractor exceeds at its own risk. The government must provide appropriate surveillance to ensure the contractor is using efficient methods and effective cost controls.
Contractors: SEA (under both the interagency agreement and direct contract) Westwood Eagle				

Source: GAO analysis of *Federal Acquisition Regulation*.

Note: Based on *Federal Acquisition Regulation (FAR)* subparts 16.4 and 16.6, as well as Energy's *Acquisition Guide*. The FAR is promulgated at 48 C.F.R. ch. 1.

Roles and Responsibilities under Interagency Agreement with SSC NOLA

The services provided by SEA were obtained by Energy through a series of agreements. Energy's interagency agreement with SSC NOLA required SSC NOLA to provide certain services to Energy. SSC NOLA carried out the agreement using an existing BPA between GSA's FTS and the contractor,

SEA. The BPA was entered into under a GSA FSS contract, and an official at GSA's FTS was the contracting officer (CO) who had authority to contract for goods and services on behalf of the government. Additionally, the CO had overall responsibility for negotiating task orders under the BPA and certifying the contractor's invoices for payment based on evidence of approval (i.e., receipt and acceptance of goods and services) by the ordering agency. The CO designated representatives of the ordering agency—in this case, SSC NOLA—to be the contracting officer's representatives (COR). The COR was authorized by the CO to perform specific technical and administrative functions. The COR was responsible for the review and approval of SEA invoices for payment by GSA. Additionally, SSC NOLA was responsible for approval of contractor travel and contract deliverables. Although authority for contract oversight and administration was delegated among multiple agencies, ultimate responsibility for the contract rested with the customer agency (receiving agency), Energy.

Although the use of interagency contracting vehicles can be beneficial because the ordering agency does not have to go through an extensive procurement process, interagency agreements must be effectively managed to ensure compliance with the FAR and to protect the government's interests. When a customer agency's contracting needs are being handled by another agency, effective internal controls are particularly critical because of the more complex environment. We, along with agency inspectors general, have reported risks associated with interagency contracting. Management of interagency contracting was added to GAO's high-risk list in January 2005.¹³ We found that roles and responsibilities for managing interagency contracts need clarification and agencies need to adopt and implement policies and processes that balance customer service with the need to comply with requirements.

Federal requirements for acquiring goods and services through contracts are found in laws and implementing regulations. The FAR prescribes uniform policies and procedures for acquisition by executive agencies. Additionally, agencies may have their own supplemental regulations, policies, and procedures for acquisition. For example, Energy has a supplemental regulation called the *Department of Energy Acquisition Regulation*, an acquisition guide, an accounting handbook, and other

¹³GAO, *High-Risk Series: An Update*, [GAO-05-207](#) (Washington, D.C.: January 2005).

guides that describe its policies regarding contracts, subcontracts, and interagency agreements.

Government Settlement Agreement and Release with SEA

On November 29, 2005, the Department of Justice (DOJ) and SEA executed a settlement agreement and release (settlement) after an investigation of allegations of improper billings by SEA of labor charges on work for SSC NOLA and its customers under a GSA FSS contract and two related BPAs covering the period from April 1999 through September 2005.¹⁴ SEA billed SSC NOLA approximately \$346 million for labor charges over this period, including approximately \$26.6 million under task orders that provided services to Energy.¹⁵ The “covered conduct” investigated by the government related to allegations of improper billing by SEA for labor in two areas: billing indirect labor costs as direct labor costs and billing for employees in labor categories for which they were not qualified. Under the terms of the settlement, SEA paid the government \$9.5 million.¹⁶ In turn, the government release provided that the government will have no further civil or administrative monetary claims or cause of action against SEA under the False Claims Act¹⁷ or any other statute creating causes of action for damages or penalties for the submission of false or fraudulent claims, or at common law for fraud or under any other statutes or under theories of payment by mistake, unjust enrichment, or breach of contract, for the covered conduct.

In this report, we did not determine whether or to what extent the terms of the settlement may affect any potential additional monetary recoveries by

¹⁴The settlement is applicable to all task orders under the two BPAs. The investigations serving as the basis of the settlement consisted of one conducted by DOJ on amounts billed from April 1999 through September 2000 and another conducted by the Naval Audit Service on amounts billed from August 2000 through September 2004. Neither of these investigations, however, included the task orders under which SEA provided services to Energy.

¹⁵Further, under a separate agreement from September 2004 through December 2004, SEA billed Energy directly for an additional \$2.6 million of labor charges for a total of \$29.2 million.

¹⁶SEA disputes the allegations at issue in the government’s investigation concerning the covered conduct, and contends that SEA’s conduct was proper and in accordance with applicable law and regulation.

¹⁷31 U.S.C. §§ 3729-3733.

the government for the questionable and improper payments made to SEA that we identified.

Internal Control

Internal control is the first line of defense in safeguarding assets and preventing and detecting fraud and errors. Internal control is not one event or activity but a series of actions and activities that occur throughout an entity's operations on an ongoing basis. It comprises the plans, methods, and procedures used to effectively and efficiently meet missions, goals, and objectives. Internal control is a major part of managing any organization. As required by 31 U.S.C. § 3512(c),(d), commonly referred to as the Federal Managers' Financial Integrity Act of 1982, the Comptroller General issues standards for internal control in the federal government.¹⁸ These standards provide the overall framework for establishing and maintaining internal control and for identifying and addressing major performance and management challenges and areas at greatest risk of fraud, waste, abuse, and mismanagement. These standards include establishment of a positive control environment that provides discipline and structure as well as the climate that influences the quality of internal control. As we reported in our Executive Guide, *Strategies to Manage Improper Payments*, a lack of or breakdown in internal control may result in improper payments.¹⁹ Improper payments are a widespread and significant problem in government and include inadvertent errors, such as duplicate payments and miscalculations; payments for unsupported or inadequately supported claims or invoices; payments for services not rendered; and payments resulting from outright fraud and abuse.

¹⁸GAO, *Internal Control: Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999). See also, GAO, *Policy and Procedures Manual for Guidance of Federal Agencies*, Title 7, "Fiscal Guidance", chs. 2, 6, and 7 (Washington, D.C.: May 1993).

¹⁹GAO, *Strategies to Manage Improper Payments: Learning From Public and Private Sector Organizations*, [GAO-02-69G](#) (Washington, D.C.: October 2001).

Energy Did Not Establish Effective Controls over Payments to Contractors or Overall Contract Costs

Energy's control environment and specific internal control activities over payments to contractors and overall contract costs were not effective in reducing the risk of improper payments. Energy did not establish an effective review and approval process for contractor invoices that enabled it to verify that goods and services billed had actually been received and charged at the agreed-upon amounts. In the case of SEA, much of the responsibility rested with SSC NOLA; however, Energy did not assure itself that these responsibilities were adequately carried out. Further, accountability for equipment purchased and reimbursed by Energy for the program by contractors was not maintained. In addition, Energy and its contracting partners, GSA and SSC NOLA, did not give adequate consideration to subcontractor arrangements, including the extent to which subcontracts were used and what amount contractors were to be paid for subcontractor work. Payments for subcontractor costs represented nearly \$15 million. Finally, Energy did not effectively monitor overall contract costs and made errors in reporting total contract costs in its internal and external financial reports. Cumulatively, these weaknesses and the poor control environment made Energy vulnerable to improper payments to contractors and precluded it from effectively managing the overall cost of the contracts.

Effective Review and Approval Process for Contractor Payments Was Not Established

Energy did not establish adequate control activities to ensure an effective process for the review and approval of contractor invoices. Specifically, contractor services were not adequately monitored, labor categories were not verified, and other direct costs were not adequately reviewed. In the case of the largest contract with SEA, SSC NOLA was responsible for review and approval of SEA invoices, but did not adequately perform this function, nor did Energy take steps to assure itself that SSC NOLA was properly carrying out its responsibilities. Further, the review and approval process used by Energy for its contracts did not include the steps necessary to validate the invoices before payment. The FAR, Energy's accounting handbook, and federal standards for internal control require review and approval of invoices in order to determine if goods and services were actually provided in accordance with contract terms and if invoiced amounts were allowable under regulation or the terms of the contract.

Contractor Services Billed Were Not Sufficiently Monitored

Proper invoice review procedures for contractor services call for an effective process to observe and monitor the services provided by contractors and ensure that timely verification of services is provided to the officials approving the invoices for payment. However, neither Energy

on its contracts nor SSC NOLA on the SEA contract conducted adequate observations and monitoring of services provided by contractors or linked the observations that were performed to invoices submitted to the government. SEA, Westwood, and Eagle provided services under time and materials task orders. The FAR states that because time and materials contracts provide no positive profit incentive to the contractor for cost control or labor efficiency, appropriate government surveillance (or monitoring) of “contractor performance is required to give reasonable assurance that efficient methods and effective cost controls are being used.”²⁰

SSC NOLA, as the COR on the SEA contract, was responsible for performing observations of services provided by SEA but did so only sporadically. The SSC NOLA Project Manager, who was located in New Orleans, stated that he made periodic trips to observe SEA services in the Washington, D.C., area.²¹ However, we determined based on our review of travel documentation that as much as 6 months passed between his trips, and that no trips were made after February 2004 when SEA more than tripled its workforce in support of OWA. Further, even when the SSC NOLA Project Manager did observe services, he did not systematically link these monitoring activities to the invoice review and approval process.

We identified a similar lack of systematic linkage of monitoring activities to the invoice review process for services provided by Eagle. Eagle operated the resource centers supporting EEOICPA activities of both Energy and DOL. Energy provided some evidence of programmatic monitoring and the receipt of quarterly financial information for Eagle’s services, but did not demonstrate how those activities were systematically linked with Energy’s review of Eagle’s monthly invoices. Without such linkage, Energy did not have adequate assurance that amounts billed reflected services actually provided and that they were billed at the correct rates.

Energy’s monitoring of services provided under the Westwood contract was also insufficient, as follows.

²⁰FAR 16.60(b)(1).

²¹Initially, SEA provided information technology services in New Orleans. Later, SEA began providing case processing activities for OWA and relocated the case processing services to Washington, D.C. The case processing services ultimately accounted for 86 percent of total SEA services provided under SSC NOLA’s BPA.

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- Physicians serving on physician panels were retained by Westwood as independent contractors. These physicians reviewed cases at their homes or at Energy headquarters and submitted invoices or time sheets to Westwood for the hours worked. Neither Energy nor Westwood had an effective mechanism in place to assess the reasonableness of the hours billed by these physicians, which totaled over \$3 million. Our review of selected physician panel invoices found that one physician reported working as many as 19 hours in a day, and these hours were not questioned by Westwood or Energy. In another example, a physician regularly billed significantly more than 173 hours a month—the average number of working hours a month based upon working 5 days a week and 8 hours a day. This physician billed 265 hours in March 2004, 210 in April 2004, 335 in May 2004, and 252 in June 2004. Westwood provided some evidence—a variety of metrics—that it considered the productivity of the physicians, such as reports that summarized hours needed to review each case, and quality metrics, such as decisions overturned and cases returned because of clerical errors. However, this approach was not effective in assessing the reasonableness of the hours billed. In fact, the productivity measures were developed based on the hours actually billed on the invoices submitted by the physicians, and therefore Energy had no independent baseline with which to measure productivity or to assess the reasonableness of hours billed on the invoices submitted by the physicians.
 - Four doctors who performed quality checks before the claims were submitted to the physician panels and again after the physician panels had made recommendations were also not sufficiently monitored. Three of the four doctors we interviewed told us that they worked independently or with only limited monitoring or supervision by Westwood. The doctors told us that they did interact with Energy technical personnel; however, these technical personnel were not involved in Energy's invoice review and approval process. The doctors submitted their invoices or other records of time worked to Westwood for payment, and Westwood then billed the government for these charges. These physicians regularly billed for 9 to 12 hours per day and as high as 18 hours per day, yet there was no evidence that these charges were validated by Westwood or questioned by Energy. Energy told us that it was aware that these doctors worked long hours. However, Energy did not systematically observe the hours worked and then compare any observations to the amounts paid for those hours, nor did it determine that Westwood was adequately monitoring these services as a basis for its billings.

Labor Categories and Certain
Other Activities Were Not
Verified against the Contract

For SEA task orders, SSC NOLA did not take appropriate steps to verify that labor hours were being billed at the appropriate rates or to determine that employees were qualified under the labor category education and experience requirements negotiated in its contracts. Further, Energy did not take steps to ensure that SSC NOLA implemented appropriate verification procedures or effective compensating control strategies. Appropriate procedures to verify labor hours may include sampling on a test or periodic basis résumés of contractor employees, including independent verification of education and work experience to requirements under the contract or detailed evaluations of labor categories at higher risk because of volume or price per hour.

In certain cases, we found that the labor categories negotiated in the contract did not reflect the actual tasks being performed, making it difficult to determine whether the labor charges were based on appropriate rates. We found that the labor categories in the contract were originally designed for information technology activities and did not reflect labor categories appropriate for the significant case development activities SEA performed in the last 2 of 3 years of SEA's task orders.²² While Energy provided us with a crosswalk of the information technology labor categories that SEA used for billing purposes to case processing job titles under the third task order, this crosswalk was not used by SSC NOLA in order to review SEA's billings. Further, the underlying BPA was not amended to reflect labor categories that matched the case development activities that SEA provided.

We found similar problems with another contractor, Westwood. The statement of work underlying the Westwood task orders from August 2001 through February 2005 provided for nine activities "supporting the Advisory Committee." However, Westwood performed the following additional activities that were significant to OWA in terms of nature and amount but were never incorporated into Westwood's statement of work:

- Implementing physician panels, which included retaining doctors and coordinating the flow of cases between panel members.

²²As discussed in the Background section, the GSA Inspector General found that two of the three task orders included case processing activities in addition to information technology activities and were therefore outside the scope of the underlying GSA FSS contract and a misuse of the contract vehicle.

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- Providing medical doctors who performed quality checks before the claims were submitted to the physician panels and again after the physician panels had made recommendations.
 - Obtaining consulting services at the request of Energy, including advisors on environmental health issues and process improvements.

Since the contract did not fully reflect actual duties that were subsequently performed, Energy did not have an adequate basis on which to determine if amounts billed for labor were appropriate and consistent with the contract terms.

Other Direct Costs Were Not Adequately Reviewed

Neither Energy for the Westwood contract nor SSC NOLA for the SEA contract performed a sufficient review of other direct costs billed under the contracts. Energy did not require Westwood to report a detailed breakdown of its other direct costs, such as travel and materials, as stipulated by its contract and did not request Westwood to submit supporting documentation for these costs except on a sporadic basis because, according to Energy, the amount of supporting documentation was “too voluminous.” Westwood billed Energy for approximately \$11.6 million of goods and services provided from August 2001 through February 2005 in support of OWA, of which approximately \$5.2 million was for other direct costs. As shown in figure 2, the amount of Westwood’s other direct costs was significant to its monthly billings but was not adequately described on the invoice.

Figure 2: Westwood Group, Inc., Invoice for Services Provided to OWA in October 2004

For the Period 10/01/2004 through 10/31/2004		The Westwood Group, Inc.		Contract No: DE-AT01-01EH01014	
				Voucher No: 2004-3-2	
				Date: 9 November 2004	
TASK 1					
LABOR CATEGORY	RATE/DPLH	DPLH THIS BILLING PERIOD	\$ CLAIMED THIS BILLING PERIOD	CUMULATIVE DPLH	AMOUNT
Project Manager			\$2,767.23		\$11,171.41
Senior Scientist			\$171,250.00		\$358,000.00
Analyst			\$8,795.52		\$34,326.96
Technical Editor			\$6,643.90		\$16,174.46
Admin. Specialist			\$58,107.16		\$126,977.96
OT			\$0.00		\$0.00
Clerical			\$0.00		\$0.00
OT			\$0.00		\$0.00
Subtotal Labor Cost		2410	\$247,563.81	5535	\$546,650.79
OTHER DIRECT COSTS					
Travel			\$30,935.76		\$51,954.17
Other Direct Costs			\$125,763.95		\$209,434.88
Temp. Labor			\$294,710.94		\$687,301.07
Subtotal ODC's			\$451,410.65		\$948,690.12
ODC INDIRECT RATE	12.00%		\$54,169.28		\$113,842.75
TOTAL INVOICE			\$753,143.74		\$1,609,183.66

Source: Westwood Group, Inc.

Note: "DPLH" stands for Direct Productive Labor Hours and represents the number of hours charged in each labor category.

Our review of the invoice documentation Energy did request and receive for one monthly invoice identified costs that should have been questioned and investigated by Energy prior to payment, but were not. In addition, we examined the supporting documentation that was available for other Westwood invoices (a majority of which Energy did not request or review

prior to payment) and identified numerous charges improperly paid by Energy. These findings are discussed later in the report.

SSC NOLA, in its role as COR and project manager on the SEA task orders, did not sufficiently review travel costs incurred by SEA. SSC NOLA preapproved travel when it determined the travel met a need of the program and then subsequently reviewed and approved the travel voucher, including all receipts submitted, after the travel had occurred. The COR also verified that travel had been preapproved, travel corresponded with the preapproved dates and location, and the amounts did not exceed the preapproved estimates. However, SSC NOLA did not question whether the costs actually incurred for airfare were reasonable and appropriate. In particular, we found instances of first-class travel and other excessive airfare costs that were not identified or questioned by SSC NOLA. For example, our analysis of the historical data supporting SEA's travel for OWA activities on its most frequently flown route (New Orleans to Ronald Reagan Washington National Airport) showed airfares as high as \$1,482 for first-class travel and as low as \$362 for coach class. SSC NOLA officials indicated that in the future they would review contractor travel costs more closely, including adding new procedures to verify that contractor travel complied with the applicable travel regulations regarding first-class travel.

Accountability for Equipment Purchased by Contractors Was Not Maintained

Energy did not have sufficient controls over the equipment, such as computers, laptops, and copying machines, purchased by its contractors for the program. The equipment, totaling nearly \$1 million, ranged from a \$160 printer to a \$17,742 copying machine. Any equipment purchased by a contractor and for which the government holds the title is considered government-owned property.²³ Maintaining accountability over assets calls for procedures to approve equipment purchases prior to purchase, steps to ensure the contractors received and safeguarded the assets during the operation of the program, and conducting timely inventories of equipment it received from each contractor at the conclusion of the program. However, Energy did not have adequate procedures in place to properly account for equipment purchased by its contractors nor did it work with SSC NOLA to ensure adequate monitoring of SEA-purchased equipment. Specifically, Energy did not have a formal process to approve Westwood equipment purchases prior to purchase. Additionally, Energy did not take

²³FAR subpart 45.5.

steps to ensure the contractor maintained accountability over equipment while it was in its possession. Further, physical inventories of Westwood and SEA purchased equipment were not completed until at least 8 months following the expiration of the respective contracts.

Our analysis of documentation supporting Westwood's invoices from January 2002 through February 2005 found that Westwood purchased over 70 pieces of computer and computer-related items costing approximately \$62,000 and was subsequently reimbursed by Energy. Energy, however, did not conduct an inventory of that equipment until December 2005, nearly 9 months after Westwood's contract expired. Further, since Energy had not previously obtained supporting documentation for Westwood's equipment purchases, Energy relied on Westwood to provide it with a listing of all items purchased. During its inventory, Energy identified 13 missing items. Our comparison of the inventory to Westwood's billings for the equipment, however, identified an additional 31 items that Westwood had not included on its listing that also needed to be accounted for. Finally, we identified over \$31,000 in computer purchases that did not contain sufficient supporting detail, such as a description of the items, serial numbers, or model numbers, to be used to determine if the items were accountable assets and, if so, if they were included on the inventory list. In response to our inquiries, Energy made an effort to locate these additional items and has indicated that several items have been found. Energy's and its contractor's lack of accountability for the equipment over an extended period put this equipment at risk of loss or misappropriation without detection.

Inadequate Consideration of Subcontract Arrangements

Energy did not consistently obtain and review subcontract arrangements or adequately consider the billing implications of the extensive use of subcontracts by its prime contractors. Nearly \$15 million of \$92 million in OWA program costs were incurred by subcontractors. However, neither Energy nor SSC NOLA for SEA exercised sufficient management oversight to be fully informed of the nature, extent, scope of services, and terms of billings to the government for these services as well as the oversight the prime contractor was to exercise over its subcontractors.²⁴ Our review of the subcontracting arrangements used by SEA and TDI identified

²⁴For example, FAR 44.201-1 and 44.201-2 provide mechanisms for agencies to consent to or be notified of subcontracting agreements prior to award of the subcontracts.

numerous subcontracting issues that were not addressed by Energy or, in the case of SEA, by SSC NOLA or GSA.

Of the \$29 million in labor billings by SEA, \$10.1 million was provided by subcontractors, including temporary staffing agencies. While Energy, SSC NOLA, and GSA were aware that SEA utilized subcontracted labor, GSA's initial consideration of the use of subcontractors was given in 2000 as part of SEA's proposal under the BPA more than a year before the Energy task orders and was not updated to reflect changes in SEA's business partners or the scope of work provided to Energy over time. To illustrate, SEA utilized 16 subcontractors to provide services to Energy, but only 5 of those subcontractors, representing approximately 6 percent of total billings for subcontractor services, were included in SEA's proposal. Further, there was no evidence that either SSC NOLA or GSA had been informed of the extent to which SEA used subcontractors to provide OWA services or the amount SEA paid for those services. SSC NOLA told us that it was concerned that SEA did not separately identify the amount of charges associated with subcontracted labor from other labor charges, but said that GSA officials told it such a breakout was not necessary. SSC NOLA did not pursue the issue again with either GSA or SEA.

Additionally, TDI billed Energy for services provided by Westwood from February 2002 through September 2004 under an arrangement that TDI and Westwood viewed as a prime contractor and subcontractor relationship. However, we found that an agreement between TDI and Westwood containing basic information, such as hourly billing rates by labor category, allowable costs, and other basic terms and conditions for the period Westwood provided services did not exist. Further, while Energy's CO told us he obtained and reviewed a price proposal submitted by Westwood for this period, Energy did not take the appropriate steps to ensure the prices were formalized into TDI's prime contract with Energy or any other binding agreement. Without an effective contractual agreement, including negotiated rates, it was not possible for Energy to adequately review the amounts TDI billed for costs attributed to Westwood.

Overall Contract Costs Were Not Effectively Monitored or Accurately Reported

Energy did not establish internal control monitoring practices to effectively manage overall contract costs, including using contract ceilings to manage and encourage cost-effectiveness. Further, Energy did not accurately report contract costs in internal and external financial reports. We identified instances of improper cost assignments between Energy programs and a payment error that understated the program's costs by

\$2.5 million. This amount includes a processing error of \$1.7 million we identified during our review that had not been previously identified by Energy.

Contract Ceilings Were Not Effectively Monitored

Energy failed to monitor cumulative contract costs adequately. Ceilings, or caps, on total contract values and on certain contract components, such as other direct costs, impose limits that help the government manage contract costs. Contract ceilings are particularly valuable tools for monitoring time and materials contracts, which have few other mechanisms for managing cost-effectiveness. Our review of contract and interagency agreement ceilings for the four major OWA contractors showed that the ceiling amounts of certain contracts were increased numerous times. For example, the amount for Westwood's total contract ceiling was modified six times, including four times during the last 9 months of the contract. However, Westwood still exceeded the cost ceiling for other direct costs by nearly \$2 million by the end of the contract. Energy paid these amounts, thereby reducing the value of the contract ceiling and further demonstrating Energy's lack of a proper control structure to manage contract costs.

Contract Cost Reporting Was Flawed

Energy also did not properly track and report contract costs in internal and external financial reports. Energy improperly assigned some costs of OWA activities to other program reporting units and, in some cases, assigned the costs of other program reporting units to OWA. For example, Energy improperly assigned the costs of OWA services provided by Westwood to other program reporting units, in effect using other programs' funds to pay for OWA activities. This occurred because Energy did not assign the costs of the invoice according to services provided to each program, but instead either divided the total cost of the invoice equally across all programs receiving services or assigned costs based upon the amount of funds available in the different program reporting units. At the end of Westwood's first contract, \$1.6 million of costs associated with OWA activities were assigned to other program reporting units, understating the OWA program costs. Conversely, Energy, using similar methods, improperly used \$2.1 million of OWA funds to pay TDI costs through its second contract that were unrelated to OWA activities, overstating the OWA program costs. Assigning costs on a basis other than the actual cost of services not only misstates program costs but also hinders the agency's ability to adhere to federal cost accounting standards.

In addition, Energy used \$1.3 million of funds from two other Energy program reporting units to pay for SEA services in fiscal years 2003 and

2004. Although the amount transferred was authorized by senior Energy management, it was not reported externally in Energy's September 30, 2004, report to Congress on EEOICPA expenditures. As a result, the cost report was understated by \$1.3 million.

We identified a total of \$5.0 million (gross) in cost assignment errors and reporting omissions. These errors, which were partially offsetting and resulted in a net understatement of OWA program costs of \$800,000, prevented the agency and other interested stakeholders from knowing the true cost of program activities at any given time.

We further identified a \$1.7 million payment error related to SEA billings that occurred in December 2004. GSA paid SEA for its services and was reimbursed by SSC NOLA. SSC NOLA then received a reimbursement from Energy through the intragovernmental payment process, but was not reimbursed for the full amount owed it because of a processing error. Neither SSC NOLA nor Energy identified the mistake. The error went undetected by Energy because it did not reconcile reimbursements made to SSC NOLA to appropriate supporting documentation in accordance with Energy accounting policy. The error understated the OWA's program costs until it was corrected in September 2005 after we brought it to the attention of the Defense Finance and Accounting Service, the Department of Defense unit that handled SSC NOLA's intragovernmental payment transactions.

Energy Made Millions of Dollars in Improper and Questionable Payments to Contractors

The fundamental internal control weaknesses associated with Energy's contract payment process contributed to \$26.4 million in improper and questionable payments to contractors that we identified as part of our review. We employed a variety of forensic auditing techniques to assess the validity of Energy payments for OWA activities and identified \$24.4 million in improper and questionable payments to contractors for direct labor billed under improper labor categories and the inappropriate use of fully burdened labor rates. We also identified \$778,613 in improper and questionable payments for other direct costs, including amounts for add-ons and base fees, and certain travel and related costs. Further, we questioned whether certain other payments toward the end of the program for furniture and computer equipment, totaling nearly \$1.2 million, were an efficient use of government funds. Given Energy's poor control environment and the fact that we only reviewed selected Energy payments, other improper and questionable payments may have been made that have not been identified.

Table 3 includes the net amount of improper and questionable payments when we could determine a net amount. We use the gross amounts paid by Energy when it was not practical for us to determine offsets or reductions that might be due to the contractors in lieu of the amounts that Energy paid. Any potentially recoverable amounts would need to be determined after consideration of any reductions or offsets.

Table 3: Summary of Improper and Questionable Payments

Type of Cost	Improper	Questionable	Total
Labor			
Labor categories ^a	\$2,498,920	\$17,686,892	\$20,185,812
Fully burdened labor rates	3,661,429	569,798	\$4,231,227
Overtime charges	3,019		\$3,019
Subtotal			\$24,420,058
Other direct costs			
Add-on charges and base fees	\$655,734		\$655,734
Per diem and commuting costs ^a	12,418	\$4,704	\$17,122
First-class travel ^a	5,207	9,119	\$14,326
Other miscellaneous payments	91,431		\$91,431
Subtotal			\$778,613
Inefficient use of government funds			
Furniture		\$821,129	\$821,129
Equipment		341,790	\$341,790
Subtotal			\$1,162,919
Total	\$6,928,158	\$19,433,432	\$26,361,590

Source: GAO.

^aThe amounts reported for these categories represent the gross amount paid by Energy to its contractors and therefore do not reflect any reductions or offsets that may be due the contractors for the goods and services that were provided. Any potentially recoverable amounts would need to be determined after consideration of these reductions or offsets.

The following sections provide additional information on the improper and questionable payments we identified.

Energy Made Improper and Questionable Payments for Labor Charges

A significant portion of OWA program expenditures was for labor provided by contractors and their subcontractors. For the four major contractors discussed in this report, Energy paid \$45.3 million for contracted and

subcontracted labor, representing approximately 49 percent of total OWA program costs reported by Energy. In light of Energy's weak controls over labor category requirements and insufficient observation and monitoring of contracted services, we performed a variety of tests on the amounts billed for labor. Our tests disclosed that certain contractors used inappropriate labor categories for billing purposes, and as a result the government made improper payments for those charges. We also found that some labor billings could not be validated because of insufficient criteria for labor category qualifications but were paid nonetheless. Additionally, Energy and SSC NOLA paid prime contractors for subcontractor labor at fully burdened labor rates instead of paying only the costs incurred by the prime contractor and also paid time and a half for certain hours worked beyond a standard 40-hour week, which was not in accordance with the contract.

Labor Categories

Westwood billed over half a million dollars of labor charges under labor categories for which the employees were not qualified to be billed. We reviewed résumés for 25 Westwood employees whose time was billed to OWA. Our comparison of employee résumés to the qualifications that were required under Westwood's contract revealed that Westwood billed for 7 employees under labor categories and at billing rates for which the employees were not qualified, resulting in \$602,000 of improper payments by Energy. For example, the analyst labor category required a college degree and at least 5 years of experience in a specific field, such as health or physical sciences or environmental studies. However, the employees we reviewed who were billed as analysts did not have college degrees or did not have the necessary years of experience. Westwood's Project Manager told us that he was unfamiliar with the minimum qualifications negotiated under the contract. Further, Westwood management officials had not previously compared the employees' qualifications to the requirements listed in the contract, but they told us they have since taken steps to screen applicant qualifications.

We also identified \$1.9 million of improper payments to SEA that resulted from the use of inappropriate labor categories by SEA. Using data mining and other forensic auditing techniques, we selected 94 individuals directly billed by SEA and requested their personnel files in order to compare education and experience qualifications to what the contract required. Because personnel are often billed under more than one labor category under the contract, the personnel files we requested represented 187 comparisons. However, as discussed later, we were only able to make 87 comparisons. For these 87, we identified the following instances of labor

costs billed under inappropriate labor categories, which resulted in improper payments by Energy.

- SEA billed approximately \$970,930 under labor categories that did not reflect actual duties performed. SEA had three consecutive program managers who functioned as the project lead and were the main liaisons between Energy and SEA officials. Yet these three managers were not billed to the government under the program manager (average billing rate of \$106/hour) or project manager (average billing rate of \$117/hour) labor rates but rather as subject matter experts, which were billed at an average rate of \$205/hour. Project and program managers, according to the labor descriptions under the contract, generally required the ability to manage contract support operations, including organizing and planning activities. On the other hand, a subject matter expert provides assistance in “enhancing the alignment of Information Technology strategy with business strategy” and “evaluates expectations for and capabilities for the information management organization.”

In November 2005, we asked SEA officials why these project leads were not billed under the less costly project or program manager labor categories, but they offered no viable explanation. On March 23, 2006, counsel to SEA told us that they disagreed with our view that these were improper payments because the three individuals’ “ability to manage was informed and enhanced by their expertise in engineering and information technology.” Further, counsel to SEA said that “given their extensive expertise in their fields, it seems appropriate for SEA to have billed these senior personnel as subject matter experts.” We disagree and find no basis for the government to have paid more for program manager labor than the agreed rate for that labor category.

- SEA also billed and Energy paid \$649,182 for services provided by four employees who were not qualified for the labor category under which they were billed. Two employees were billed as systems engineers (average billing rate of \$85/hour) who did not meet the minimum 5 years programming experience. They had 3 years or less of general computer experience. A third employee did not have the years of experience necessary to be billed as a case management technician, which required a minimum number of years of medical records experience. The fourth employee was billed as a senior computer scientist at an average billing rate of \$117/hour, but the documentation maintained in the employee’s file did not provide adequate evidence that the employee met the minimum 5 years of programming experience.

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- Charges for two other SEA employees, totaling \$276,808, were billed as graphics illustrators, although the job descriptions for these employees indicate that they performed administrative support services, for example, project scheduling, support activities, and making travel arrangements and preparing travel-related paperwork. We found no basis for these employees to be billed as graphics illustrators at an average billing rate of \$52/hour. Further, because general and administrative costs, such as those associated with the administrative duties performed by these two employees, are recoverable through a component of the fully burdened labor rates used under the time and materials task orders, the costs associated with these two administrative employees may be duplicative.

Of the 187 total comparisons we initially planned to make, 72 comparisons were not possible because certain labor category descriptions negotiated for use under the BPA lacked sufficient criteria for assessing whether a person was qualified to be billed at that labor category. In total, we identified about one-third of the labor categories used by SEA, representing \$15.6 million in questionable payments by Energy, that did not include sufficiently explicit descriptions of the requirements and duties of the position for us to assess the appropriateness of the labor amounts billed for these labor categories. For example, the description for senior management analyst listed desirable skills and knowledge in the areas of business and mathematics, for instance, but did not list education or years of experience requirements. SEA billed \$7.2 million, at an average hourly billing rate of \$90/hour, under that labor category. We found that billings in this labor category included amounts for case processors (who generally were registered nurses or had medical backgrounds) and records management personnel (who generally had degrees in business or records management).

Based upon discussions with both SEA and SSC NOLA officials and our review of the BPA and underlying GSA schedule contract, we found that labor categories reflecting the necessary duties, education, and skills Energy required for the work performed did not exist under the GSA contract, which was originally let solely for information technology activities. Instead, SEA used labor categories that “best fit” the work performed and that had what SEA considered to be an appropriate billing rate for the services provided. GSA as the contracting officer did not amend the contract to align labor category descriptions with the needs of the government. While Energy developed a crosswalk of labor categories to case processing job titles, this crosswalk did not specify skills or education

qualifications that would supplement those originally provided for under SEA's contract.

Further, an additional 28 labor category comparisons could not be made because SEA either did not obtain or had not retained résumés and other documents that evidenced independent validation by SEA (or confirmation of validations performed by others) of employee skills, work experience, and education requirements for personnel it obtained through temporary hiring agencies or other subcontractors. The 28 comparisons we made in our review represented a portion of the \$10.1 million in subcontracted labor charged the government. After removing other improper and questionable amounts noted elsewhere in this report to prevent double-counting, we consider \$2.1 million of subcontracted labor billings to be unsupported and therefore questionable payments by Energy. Without this information, it would not be possible for us or others to determine if these temporary personnel were billed under appropriate labor categories and at appropriate billing rates.

Fully Burdened Labor Rates

SEA and Westwood used fully burdened labor rates that included base wages plus fringe benefits, overhead costs, and profit to bill for subcontracted labor but had no basis to do so under their contracts. This practice resulted in over \$4 million in “markups” on subcontracted labor charges that were paid by Energy. Based on our analysis, Energy should have paid only incurred costs for the subcontracted labor, which represented amounts paid by the prime contractors for labor obtained from temporary staffing agencies, other subcontractors, or independent contractors. The following is a discussion of SEA and Westwood billing practices and the resulting improper and questionable payments by SSC NOLA and ultimately Energy.

SEA

Over 40 percent of SEA's direct labor hours were provided by labor obtained under arrangements with temporary staffing agencies. In total, from December 2001 through December 2004, SEA paid subcontractors, including temporary staffing agencies, \$6.86 million for the services. Instead of billing the government for this amount, SEA billed the government \$10.08 million for these services under fully burdened labor rates, resulting in a markup of \$3.22 million and improper and questionable payments by SSC NOLA and ultimately Energy.

Energy inappropriately paid \$7.12 million for work costing SEA \$4.47 million that was not contemplated at the time the labor rate negotiations occurred. As previously noted in the background section, the GSA Inspector General reviewed the three Energy task orders for SEA services and reported that the case development activities performed by temporary staffing agencies under the second and third task orders were outside the scope of the underlying GSA FSS contract and a misuse of the contract vehicle that was designed for information technology services. These two task orders represented approximately 83 percent of total SEA services provided to Energy. Because the services were outside the scope of the underlying FSS contract, there was no basis for SEA to bill for the subcontracted services at other than cost.

The contracting officer may add items not on the FSS only if all applicable FAR requirements are followed. These requirements include publicizing the government's proposed contract action (FAR part 5), complying with the full and open competition requirements (FAR part 6), and meeting the source selection requirements (FAR part 15). In addition, the contracting officer should determine that the price of the items or services not on the underlying GSA schedule contract—here, case processing activities performed by labor obtained through temporary staffing agencies—is fair and reasonable. None of these requirements were satisfied for the \$7.12 million of payments to SEA. Given that the FAR requirements were not met for this out-of-scope work, the schedule rates were inapplicable. Accordingly, the \$2.65 million markup of subcontractor rates over cost was not properly supported and was improper.

SEA also billed for subcontracted services that were within the scope of work of the underlying contracts and task orders but may have been inappropriately paid by Energy using fully burdened labor rates. The time and material payment clause included in the SEA contracts, FAR 52.232-7,²⁵ states that “the Government will limit reimbursable costs in connection with subcontracts to the amounts paid for supplies and services purchased directly for the contract.” SEA paid \$2.39 million for the subcontracted labor under these agreements but billed the government \$2.96 million for a markup over cost of \$569,798. There are currently differing views in the contracting community (including government agencies) regarding how the payment clause is to be applied by contracting agencies when paying contractors for services provided by their subcontractors when the

²⁵48 C.F.R. § 52.232-7.

contract is otherwise silent on this matter. The clause provides that based on invoices or vouchers approved by the CO, the contractor will be paid an hourly rate amount “computed by multiplying the appropriate hourly rates prescribed in the Schedule by the number of direct labor hours performed. The rates shall include wages, indirect costs, general and administrative expenses, and profit.” The clause also provides that reimbursements to contractors for subcontractor services shall be limited “to the amounts paid.”

The view of some in the federal contracting community is that prime contractors are to be paid for subcontractor labor based on the approved fully burdened labor hour rates as if the prime contractor provided the services directly through its employees, since these are the rates the government agreed to pay for each labor category. Another view is that contractors are to be reimbursed only for what they pay their subcontractor for services. An amendment to the FAR has been proposed that attempts to clarify the application of the clause.²⁶ For the purpose of this report, we have identified payments in the amount of \$569,798 as questionable based on the literal application of this clause with regard to reimbursement to contractors for subcontractor services.

Westwood

Westwood paid four independent contractors \$2.23 million for services provided, yet billed Energy \$3.24 million using fully burdened labor rates for a markup of \$1.01 million. On October 21, 2002, Energy modified its contract with Westwood to provide for a new labor category, senior scientist, to be billed at a fully burdened labor rate of \$250/hour. The senior scientists were doctors who performed quality assurance review checks over the case files before and after the files entered physician panel review. Energy officials advised us that they negotiated this labor category and the high hourly rate in order to ensure that they had full access to the medical specialists necessary to meet the increased case-processing demands of the program. Despite this fact, and that Westwood, in its cost justification to add the senior scientist labor category, indicated that the senior scientists would be added as employees, Westwood engaged them to work as independent contractors.

²⁶See, FAR cases 2004-015 and 2003-027 at 70 Fed. Reg. 56314 and 56318, respectively, September 26, 2005.

When we inquired about the employment status of the senior scientists, Westwood's President told us they were full-time employees. However, the documents we reviewed, including written agreements between the senior scientists and Westwood, showed that Westwood engaged the senior scientists as independent contractors at hourly rates ranging from \$110/hour to \$200/hour and they were ineligible to participate in benefit packages. In response to our request for Internal Revenue Service (IRS) Form W-2, Wage and Tax Statements, for the senior scientists, Westwood provided us instead with IRS Form 1099—MISC. Form 1099 is used to report amounts paid to independent contractors, not employees. Because Westwood engaged these personnel contrary to the negotiations with Energy and the terms of the contract, Westwood inappropriately billed the government, and Energy improperly paid a \$1.01 million markup for these services.

Overtime Charges

Westwood billed and Energy improperly paid for hours beyond a standard workweek at one and a half times the billing rate for the labor category under the contract. Under its time and materials task orders, hours worked were to be billed under the labor rates negotiated in the contract, and no provision was made for overtime rates. Over the 4 years Westwood provided services to OWA, it billed Energy for 168 hours at time and a half for an incremental difference over the regular labor rate of \$3,019. Westwood's President told us that the overtime payments were verbally approved and allowed by Energy, which was evidenced by Energy's approval of Westwood invoices that clearly showed the number of hours billed at time and a half. However, Westwood's contractual agreement was not modified to reflect this approval.

Energy Improperly Paid Contractor Fees and Other Direct Costs

Other direct costs, such as travel, purchases of equipment, and add-on rates and base fees, for the four major contractors in this report totaled approximately \$10 million, or 11 percent, of total OWA program costs reported by Energy. These costs are subject to a variety of terms and conditions contained in the contracts and in the FAR. For example, allowable fees are negotiated specifically for each contract. Also, the contracts may have incorporated either the *Federal Travel Regulation* (FTR) or the *Joint Travel Regulations* used by the Department of Defense, which define allowable travel costs. For time and materials contracts, FAR 16.601(a)(2) and (b)(2) limit other direct costs to those separately identifiable from costs included in its fully burdened labor rate. Because of the weaknesses in Energy's invoice review process identified in this report, specifically the weaknesses related to Westwood's invoices, and the

significant amounts of other direct costs billed to the government by both SEA and Westwood, we obtained and reviewed the supporting documentation for selected other direct costs these two contractors billed the government. We also analyzed the fees TDI billed the government on its invoices. We identified the following questionable and improper payments.

Add-on Rates and Base Fees

Energy made \$557,429 in improper payments to Westwood for amounts the contractor added to billings for other direct costs in the form of a 12 percent add-on rate. However, there is no provision in the contract to justify such a charge. The contract provides that other direct costs were not to exceed \$120,000 in the base year, and did not provide for additional amounts, such as fees, profits, or add-on rates. Additionally, when determining the “best value” among the proposals provided in response to Energy’s solicitation for the work, Energy deemed Westwood’s proposal of a flat amount for other direct costs (with no add-on rates) to be in conformance with the solicitation while a competitor’s addition of an add-on rate for general and administrative expenses was deemed contrary to the solicitation.

Energy also improperly paid \$98,305 in base fees to TDI. The base fee is negotiated up front by Energy and TDI. It was calculated based on the level of effort provided under the contract and was limited to 3 percent of the estimated cost (\$2,761,581) for a total of \$82,847. The contract did not distinguish between the level of effort provided by TDI and any other contractor that TDI viewed as its subcontractor, including Westwood. Westwood, in addition to its previously discussed prime contract with Energy, provided services through TDI in what TDI and Westwood viewed as a prime–subcontractor relationship.²⁷ From March 2002 through September 2004, TDI billed Energy for \$181,152 in base fees that according to TDI, represented base fees for both TDI and Westwood. Because the base fee under the prime contract was limited to \$82,847, TDI overbilled and Energy improperly paid \$98,305.²⁸

²⁷Westwood’s services were significant to TDI’s billings from March 2002 through September 2004, accounting for 30 percent of its billings for OWA activities and over 40 percent of total TDI billings.

²⁸The excessive base fee also resulted in another violation of TDI’s contract terms, which limited the total amount of base fee and award fees to 10 percent of the estimated cost of the contract. The base fee and award fees TDI billed Energy equaled 12.49 percent of the estimated cost of the contract. Further, TDI received \$89,296 out of the total amount of \$181,152 as its own base fee, exceeding the contract amount by \$6,449.

Per Diem, Commuting, and
Travel Costs

Energy paid \$12,418 for per diem and commuting costs billed by Westwood related to the physician panels that were not allowed under Westwood's task orders, which incorporated the FTR.²⁹ For example, Energy improperly paid Westwood for per diem and commuting expenses of physicians who lived in the local area and per diem to out-of-town physicians for days that their own time records showed they did not work (sometimes weeks at a time). We considered an additional \$4,704 in payments to be questionable because they were not properly supported in order to determine whether the amounts billed were in accordance with the FTR.³⁰

Energy also made \$14,326 in improper and questionable payments for first-class airfare purchased by SEA. First-class airfare is prohibited by SEA's task orders that incorporate the *Joint Travel Regulations* except under certain circumstances, and those circumstances must be clearly documented in the travel voucher. Energy improperly paid \$5,207 in airfare when at least one leg of the trip was first class and was not justified in the travel documentation supporting the trip. We also questioned payments of an additional \$9,119 in first-class airfare. The travel documentation supporting these airfare costs contained some explanation for the use of first class generally related to availability. For example, one traveler noted "only first class available." However, the travel regulations state that travelers should determine travel requirements in sufficient time to reserve and use coach accommodations.³¹ Therefore, we question whether the travelers' justifications were sufficient under the terms of the contract.

Other Miscellaneous Payments

We identified \$91,431 in other miscellaneous payments that Energy improperly made to Westwood and TDI. Of this amount, \$45,631 was made for duplicate and erroneous billings from Westwood. In one case, we found that Westwood billed the government multiple times for the same cost for a physician serving on review panels. The duplicate amounts for this one physician equaled \$28,783. Westwood also billed Energy for a plane ticket

²⁹We reviewed the supporting documentation for the costs of 6 of 167 panel physicians. We chose these 6 physicians for detailed review because of either the high volume of their charges or unusual charges that we noted in our preliminary reviews of supporting documentation. We only considered their billings for fiscal year 2004, the year of the highest physician panel activity.

³⁰41 C.F.R. § 301-11.1(c).

³¹*Joint Travel Regulations*, CC2204(B)(1)(b).

that was never used and subsequently credited back to Westwood (\$643) by the airline and therefore should not have billed to Energy. These duplicate and erroneous billings were likely not identified prior to payment because Energy did not regularly obtain documentation supporting Westwood's invoices or sufficiently review the documentation it had received.

Additionally, TDI billed the government twice for work provided by its subcontractor, Westwood, during the month of April 2004 instead of billing the subcontractor's April and May 2004 invoices. The subcontractor's April invoice included more costs than its May invoice; therefore, Energy improperly paid an incremental amount of \$19,277.

Energy also improperly paid at least \$26,523 in other costs billed by Westwood that were not permitted under the terms of the contract and the FAR. The payments included \$21,172 for monthly phone bills, \$4,603 for staff parking permits, and \$748 for water cooler rentals.

Purchases of Certain Furniture and Equipment May Not Have Been an Efficient Use of Government Funds

We identified \$1,162,919 in purchases of furniture and equipment and related storage costs that may not have been an efficient use of government funds given that Congress was giving consideration to transferring responsibility for the program to another agency.³² As part of our review of overall program costs, we noted a significant increase in program costs during the last 6 months of the program beginning in July 2004. For example, the amount of SEA's invoices increased approximately 87 percent from a monthly average of \$1.2 million for the 6 months prior to July 2004 to \$2.3 million for the following 3 months. The increase in program spending followed a June 2004 transfer of \$21.2 million to OWA. According to Energy officials in a March 2004 testimony before the Senate Committee on Energy and Natural Resources, Energy transferred the funds in part to reduce the backlog of unprocessed applications by increasing the number of case developers and assistants as well as the number of physicians serving on the review panels.

In July 2004, Energy ordered \$748,409 of modular furniture that was to be installed in new work space to be occupied by claims processing personnel

³²In June 2004, the Senate passed an amendment to the fiscal year 2005 Defense Appropriations bill that would have transferred the administration of EEOICPA Subtitle D to DOL. Ultimately, the bill that was signed into law on October 28, 2004, repealed Subtitle D and replaced it with Subtitle E, which is administered by DOL. (Pub. L. No. 108-375.)

provided by SEA. However, by August 2004, OWA had initiated a hiring freeze. According to the program manager at the time, Energy was unable to cancel the furniture order and the furniture was received in September 2004. Energy paid \$6,060 a month through fiscal year 2005 to store the furniture at a storage facility, incurring costs of \$72,720 for 12 months. (See fig. 3.) We noted that Energy prepaid the manufacturer \$50,000 of installation charges in 2004 even though the furniture was in storage for 12 months and not installed until February 2006, over a year and a half later, for use by another Energy program. Total costs associated with the furniture were \$821,129, which we have classified as a questionable use of government funds.³³

³³Storage costs from October 2005 through December 2005 were paid by Energy's Office of Operations, Office of Space Management and Facilities Development Group.

Figure 3: Unused Modular Furniture in Storage Facility



Source: GAO.

During this period of increased program spending, SEA more than tripled its workforce supporting OWA at the direction of Energy. To equip these personnel, SEA purchased and subsequently billed the government for 200 desktop computers, 5 laptop computers, 6 industrial copiers, and 4 fax machines at a cost of \$341,790. This equipment was ordered from June 21, 2004, through July 27, 2004, and SEA received all items by August 2004. Because the program ceased new case processing and SEA began

downsizing its staff in November 2004, SEA only used these items in support of the program for at most 5 months. According to Energy officials, Energy took possession of the equipment from the contractor when SEA's contract ended on December 31, 2004. At the time of our inquiry nearly 8 months later, however, 134 items, with a cost of \$241,725, were still unused and located in storage rooms at Energy or could not be located.

Conclusion

The questionable and improper payments we identified during our review represent nearly 30 percent of total program funds spent through September 30, 2005. Given the lack of fundamental internal control over the payment, monitoring, and reporting of contractor costs, and the fact that we did not review all program payments, the amount of improper and questionable payments could be even greater. Further, the control weaknesses at Energy and SSC NOLA could be indicative of more systemic problems at both organizations that could put other program funds at risk. Correcting these problems will require a major reassessment of existing practices, policies, and procedures and the overall control environment. The success of this effort will depend on the level of commitment by senior management in setting the "tone at the top" and working proactively to see that the needed changes are effectively implemented.

Recommendations for Executive Action

We are making 16 recommendations to address the issues identified in this report. We are making 14 recommendations to Energy to (1) improve controls over the review and approval process for contractor invoices; (2) strengthen accountability for government-owned equipment purchased by contractors; (3) improve reporting and control of overall contract costs, including subcontractor costs; and (4) pursue opportunities for recovery of improper and questionable costs identified in this report. We are also making 2 recommendations to SSC NOLA to reassess its procedures for carrying out its responsibilities for delegated contract administration in connection with interagency agreements.

To improve Energy's controls over its review and approval process for contractor invoices, we recommend that the Secretary of Energy instruct the Deputy Secretary to:

- Develop an assessment process to use as a basis for determining reliance on and monitoring the performance of other federal agencies that perform key contract management functions on Energy's behalf,

such as monitoring contractor services, review and approval of invoices, and approval of subcontractor agreements.

- Establish policies and procedures for an effective review and approval process for contractor invoices, including (1) conducting and documenting observations (surveillance) of services provided by contractors, (2) linking those observations to the invoice review and approval process, (3) verifying labor hours are billed at appropriate rates and that employees are qualified to perform the work consistent with the terms of the underlying agreement, and (4) ensuring other direct costs are properly supported and reviewed prior to payment.
- Develop guidance for CORs or other payment/review officials that detail appropriate steps for review and approval of invoices and appropriate documentation of that review process.
- Require timely and periodic reviews of contractual agreements, especially time and materials contracts or task orders, including the statements of work, to ensure that agreements continue to reflect both the work that is being performed and the needs of the agency.

To strengthen Energy's accountability for contractor-acquired government property, we recommend that the Secretary of Energy instruct the Deputy Secretary to establish or reinforce existing policies and procedures to:

- Approve contractor equipment purchases prior to purchase.
- Verify that contractors receive and safeguard the assets during the operation of the program, including physical inventories or some other process to validate that all assets paid for are accounted for.
- Timely conduct physical inventories of contractor-acquired government property upon taking possession of the equipment at the close of contract, including resolving with the contractor any missing or defective items.

To improve Energy's reporting and control of time and materials and cost reimbursement contract costs, including subcontractor costs, we recommend that the Secretary of Energy instruct the Deputy Secretary to establish or reinforce existing policies and procedures to:

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- Review subcontracts, including those for labor obtained through temporary staffing agencies.
 - Require contractors to obtain formal approval in advance for significant new subcontract agreements or changes to existing subcontract agreements, such as significant changes in the nature, scope, or amount of subcontracted activities, including labor obtained through temporary staffing agencies.
 - Systematically monitor overall contract costs and require documented justifications from contractors for increased ceiling amounts, as well as specific documentation to support Energy's approval of the increases before incurrence of any costs beyond the ceiling.
 - Properly assign costs incurred to the correct program at the time of payment and accurately report such costs in internal and external financial reports.
 - Reinforce requirements for reconciliation of intragovernmental payments for amounts due under interagency agreements to appropriate supporting documentation.

To pursue opportunities for recovery of improper or questionable costs identified in this report, we recommend that the Secretary of Energy in coordination with the Administrator of General Services and, in relation to SEA costs, the Commanding Officer, Space and Naval Warfare Systems Center, New Orleans, to:

- Determine, in consultation with DOJ, the amount, if any, of potentially recoverable costs associated with the improper and questionable payments for labor associated with SEA that we identified in this report in light of the settlement agreement dated November 2005.
- Determine whether the other improper and questionable payments of contractor costs, including payments to SEA that are identified in this report, should be reimbursed to Energy by any contractor.

In light of the findings in this report, we recommend that the Commanding Officer, Space and Naval Warfare Systems Center, New Orleans, reassess the organization's procedures for carrying out its delegated responsibilities in connection with interagency agreements for delegated contract administration responsibilities, including the following:

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- Assess the adequacy of the review and approval process for contractor invoices, including (1) oversight and monitoring of contractor services and linkage of these activities to the invoice review and approval process, (2) verification that labor hours are billed in the appropriate categories at the appropriate rates, and (3) determining that contractor travel and other direct costs are in accordance with the contract and applicable federal regulations.
 - Establish policies to document guidance sought from GSA and the direction received on all matters of substance, including the use and billing implications of subcontracted labor, and to communicate the direction provided by GSA to the customer agency (e.g., Energy) for consideration by the customer.

Agency Comments and Our Evaluation

In the letter transmitting its detailed written comments on a draft of this report, Energy stated that it agreed with the spirit and intent of our recommendations and that it will give careful consideration to each of them. Energy also said it would revise its current policies or procedures as appropriate and described corrective actions it had already undertaken to improve its controls, including those over interagency contracting. In its detailed comments, Energy agreed with some of our findings and disagreed with others without specifically commenting on any of the 16 recommendations, including the 14 directed to Energy. In particular, Energy (1) disagreed with our view that it was ultimately responsible for the issues that we identified relating to payments and controls for SEA, a contractor obtained through an interagency agreement; (2) stated that it was engaging the Defense Contract Audit Agency (DCAA) to audit the costs of two contractors that we reported as having a number of issues related to improper payments, and that it considers this to be a control that addresses some of our findings; (3) disagreed with our findings that Energy improperly paid \$557,429 to Westwood for add-on rates and \$98,305 to TDI for base fees; and (4) stated that its June 2004 transfer of \$21.2 million was proper and that the large purchases of furniture and equipment near the end of the program were also proper. Energy also observed that the November 29, 2005, settlement and release between the government and SEA would appear to preclude the recovery of any additional money from the contractor for the improper and questionable payments that we identified in this report.

In written comments reprinted in appendix III, SSC NOLA stated that it concurred with the two recommendations calling for it to reassess its

procedures for carrying out its responsibilities in connection with interagency agreements and that it expects to complete actions on both recommendations by August 1, 2006. SSC NOLA separately provided technical comments, which we have incorporated as appropriate.

Energy took issue with a number of our findings related to SEA contract payments because Energy did not agree that it had ultimate responsibility for the contract with SEA. Energy stated that it was the responsibility of the contractor to comply with the terms of its contract. Energy stated that it is a customer of SSC NOLA and, as such, had no direct contractual relationship with the contractor, SEA. Energy's position is that SSC NOLA was responsible for conducting appropriate oversight and administration of contractor costs and that it had relied on SSC NOLA and GSA to ensure that SEA complied with the terms of its contract. Energy further stated that it deferred to SSC NOLA and GSA on issues with the SEA contract such as labor categories, billing rates, qualifications of personnel, and subcontractor arrangements and that those issues were the responsibility of SSC NOLA and GSA, not Energy.

We disagree with Energy's position that it had no responsibility as it relates to the propriety of the payments made to SEA. As discussed in the Background section of our report, in cases where authority for contract oversight and administration is delegated among multiple agencies, ultimate responsibility for the contract rests with the customer agency (receiving agency), in this case Energy. Energy cannot assign or delegate away its responsibilities³⁴ through interagency agreements; the ultimate responsibility for ensuring the success of the contracted efforts as well as the propriety of payments remains with the receiving agency. In particular, the Economy Act requires that agencies ordering and paying for services under Economy Act agreements are responsible for ensuring that they receive the required services and pay for actual costs that were incurred by the performing agency, in this case SSC NOLA.³⁵ While Energy may not have had sole responsibility for ensuring that payments made to SEA were proper, Energy was responsible for making sure that others were adequately conducting work on its behalf to ensure that program funds were not used to make questionable and improper payments.

³⁴GAO, *Principles of Federal Appropriations Law*, vol. 4, 2nd ed., pp. 15-69 through 15-70, GAO-01-179SP (Washington, D.C.: March 2001).

³⁵31 U.S.C. §§ 1535, 1536 and chapter 2 of title VII of GAO's *Policy and Procedures Manual for Guidance of Federal Agencies* provide guidance on agencies' responsibilities.

Notwithstanding its stated view that it was the responsibility of others and not Energy to conduct appropriate oversight and administration of the SEA contract, Energy stated that it did conduct observations and monitoring of SEA services. Energy further stated that it linked those observations to amounts billed each month through multiple levels of metrics and the contractor's monthly cost report. However, we found that Energy did not receive any of the SEA billings under the interagency agreement. Also, we found that Energy had no processes in place to link the cost reports, any metrics it may have produced, or any observations it may have made to amounts that the contractor billed each month. Further, because information in the contractor's monthly cost report was not compared to amounts billed each month, the procedures Energy described in its comments would be of limited value as a control process against improper payments and would not provide Energy with the necessary assurance that amounts subsequently paid to the contractor were appropriate.

In response to a number of our findings related to improper payments made to Westwood and TDI, Energy stated that it is currently having DCAA audit these contracts. Energy further stated that these audits were initiated as part of its "normal course of business" and anticipated that many of the issues we cited would normally be identified as part of a DCAA audit. While we agree that a DCAA audit of contract costs can provide a detective control to help determine whether contractor costs were proper, reliance on an after-the-fact audit is not an acceptable replacement for the type of real-time monitoring and oversight of contractor costs-preventive controls that we found to be lacking at Energy. Further, a DCAA audit of civilian contractor costs is not automatic and requires an additional cost to the government to procure. In addition, as stated in our report, the numerous issues that we identified with Westwood and TDI occurred over a 4-year period. It is important that Energy establish a control environment that includes control activities that prevent questionable or improper payments to begin with or that detects them soon after they occur so that they can be resolved in a timely manner, thus ensuring program funds are fully available to achieve the purposes of the program. Reliance on an audit by DCAA in 2006 or later of contractor activity that began in 2001 is not an efficient or effective approach to implementing proper internal controls over payments to contractors.

Energy disagreed with our findings that it improperly paid \$557,429 to Westwood in the form of a 12 percent add-on rate and also improperly paid \$98,305 to TDI for base fees. Energy stated that Westwood had an approved rate of 13 percent for general and administrative expense that was verified

by the CO in a DCAA pre-award audit. However, we found that the 13 percent general and administrative expense that Energy refers to was evaluated in the context of a price proposal for a cost plus contract. Further, under time and materials contracts like this one, general and administrative expenses are typically included in the hourly rate associated with each labor hour. While FAR 52.232-7 allows for “reasonable and allocable” material handling costs, including general and administrative expenses, for materials and subcontractors to the extent that they are “clearly excluded from the hourly rate,” neither Westwood nor Energy provided evidence during our review that any such costs were clearly excluded from Westwood’s labor rates. Therefore we stand by our conclusion that the 12 percent add-on rate to Westwood’s time and materials contract was improper.

With respect to the improper payment to TDI of \$98,305 in base fees, Energy stated that our approach of adding TDI’s fee to the fees associated with its subcontractor (Westwood) was not appropriate because there is no “base fee” in Westwood’s contract. Energy’s stated basis for its position was that the TDI contract was a cost-plus-award-fee type while TDI’s subcontract with Westwood was a cost-plus-fixed-fee type contract, with no base fee. However, as stated in our report, TDI did not have a subcontract or other binding agreement with Westwood for services Westwood provided to Energy that TDI subsequently included on its invoices to Energy. Further, Energy’s contract with TDI limited the amount of base fees to \$82,847 applied to the level of effort (i.e., labor hours billed) provided by TDI and made no distinction between hours incurred by the prime contractor or any contractor viewed as a subcontractor. Thus, the contract terms necessitate considering, as we did, the base fees of TDI and Westwood together. As stated in our report, Energy paid a total of \$181,152 in base fees when the maximum should have been \$82,847, thus resulting in improper payments of \$98,305.

Energy stated that the information in our report showing that \$21.2 million in funds was transferred to OWA in June 2004 during the same time that legislation was moving through Congress to transfer the administration of the program to DOL implies that Energy’s ramp-up activities were unsupported. Energy also stated that using these funds to purchase furniture and equipment in the summer of 2004 was consistent with congressional approval of its reprogramming actions.

Our report does not imply that Energy’s ramp-up activities were unsupported. Our report provides extensive background information on

the program, including the June 2004 transfer of \$21.2 million in funds to OWA in an effort to clear the backlog of claims. This background information was provided for context. As discussed in our report, however, we did identify \$1,162,919 in purchases of furniture and equipment and related storage costs that may not have been an efficient use of government funds given that Congress was giving consideration to transferring responsibility for the program to another agency. As discussed in the report, Energy ordered \$748,409 of modular furniture in July 2004 that was to be installed in new work space to be occupied by claims processing personnel provided by SEA. However, by August 2004, OWA had initiated a hiring freeze and therefore placed the furniture in a storage facility, incurring costs of \$72,720 for 12 months. Further, Energy paid the vendor \$50,000 up front in 2004 for installation charges even though the furniture was not installed until February 2006, over a year and a half later, for use by another Energy program.

Regarding our recommendation that Energy pursue opportunities for recovery of labor and other SEA costs that we identified as improper or questionable, Energy stated that the November 29, 2005, settlement agreement and release between the government and SEA would appear to preclude the recovery of any additional moneys for expenditures in support of Energy's programs. Our report stated that we did not determine whether, or to what extent, the terms of the November 29, 2005, settlement and release with SEA may affect any potential additional monetary recoveries by the government for the questionable and improper payments made to SEA that we identified. We also stated in our report that the release clause of the settlement is limited to "covered conduct" investigated by the government related to two areas: billing indirect labor costs as direct labor costs and billing for employees in labor categories for which they were not qualified. It is important that Energy consult with DOJ in order to determine the recoverability of funds from SEA before concluding that the funds are not recoverable. Therefore, we reaffirm our recommendation.

Discussions on other matters are provided following Energy's comments, which are reprinted in appendix II. SSC NOLA's comments are reprinted in appendix III.

As agreed with your offices, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its date. At that time, we will send copies to the Secretary of Energy and the Commanding Officer of SSC NOLA and interested congressional

committees. Copies will also be made available to others upon request. In addition, the report will be available at no charge on the GAO Web site at <http://www.gao.gov>.

If you or your staffs have any questions about this report, please contact me at (202) 512-9508 or calboml@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Major contributors to this report are acknowledged in appendix IV.



Linda M. Calbom
Director, Financial Management and Assurance

Scope and Methodology

For this review, we considered costs recorded by the Office of Worker Advocacy (OWA), the Department of Energy (Energy) office tasked with administering Subtitle D of the Energy Employees Occupational Illness Compensation Program Act of 2000 (EEOICPA) from October 2000 through September 30, 2005. Our review focused primarily on costs incurred under contracts for services by four contractors: Eagle Research Group, Inc. (Eagle); Science and Engineering Associates, Inc. (SEA); Westwood Group, Inc. (Westwood); and Technical Design, Inc. (TDI). In total, payments made to these contractors represented approximately \$55.5 million, or 60 percent, of total program costs reported by the EEOICPA program through September 2005. Our work did not extend to the program costs for claims research activities at Energy facilities. These activities were performed by Energy's major facility operating contractors that are subject to audit by Energy's Inspector General and to other reviews by Energy's financial management officials.

To assess the reliability of OWA cost data for purposes of our review, we reviewed reconciliations of OWA costs to amounts in the audited Statements of Net Cost for fiscal years 2001 through 2004.¹ In addition, for all OWA cost data for the period October 2000 through September 2005, we (1) obtained electronic files of OWA costs and performed electronic testing for obvious errors in accuracy and completeness, (2) reviewed supporting documentation for selected payments to contractors and other vendors and compared them to OWA cost data, and (3) reviewed documentation obtained from selected contractors of cumulative billings for OWA costs and compared these amounts to OWA cost data. Except for the cost tracking and reporting issues identified in the internal control section of this report and the questionable and improper payments that we identify, and the effect of any future actions taken by the agency to recover any improper payments, the OWA cost information we reviewed is considered reliable for purposes of this report. We performed the majority of our work in Washington, D.C., at Energy and Westwood. We also performed work at

¹For these years, Energy received an unqualified opinion on its financial statements. In April 2005, Energy implemented a new financial management system. A significant number of conversion, posting, reconciliation, and reporting issues associated with the conversion hindered Energy's ability to ensure the accuracy and completeness of the financial statement balances. As a result, Energy's auditors issued a disclaimer of opinion for fiscal year 2005. Four percent of OWA's program costs were initially recorded in Energy's new financial management system, and therefore the conversion does not have a material effect on the usability of the data for purposes of our report.

SEA and TDI offices in Albuquerque, New Mexico. Additionally, we observed Energy's furniture inventory located in Laurel, Maryland.

To determine whether Energy's internal controls provided reasonable assurance that improper payments to contractors would not be made or would be detected in the normal course of business, we used *Standards for Internal Control in the Federal Government* as a basis to assess the internal control structure—control environment, risk assessment procedures, control activities, information and communications, and monitoring efforts of Energy over its OWA program. Further, we reviewed contractual agreements, including prime contracts with four contractors; Energy's interagency agreement with the Space and Naval Warfare Systems Center, New Orleans, (SSC NOLA); and certain subcontract agreements provided by prime contractors. We also considered (1) prior GAO reports on the EEOICPA program, Subtitle D; (2) the results of the reviews by the inspectors general of the General Services Administration (GSA) (concerning SSC NOLA's use of SEA's schedule contract) and Energy (concerning Energy's use of interagency agreements); and (3) a prior audit report of the Naval Audit Service concerning SEA services provided to SSC NOLA. We obtained and reviewed current Energy policies regarding contracting and financial management matters, including Energy's *Acquisition Guide* and accounting handbook. We also conducted interviews with program, procurement, and financial management personnel regarding policies and procedures that were in place over contract payments, and walk-throughs of key processes, such as the invoice review and approval process, to gain an understanding of Energy's controls over contract payments. We conducted similar interviews with SSC NOLA and GSA officials to assess Energy's contractual relationship with its federal contracting partners. We compared Energy's controls to those recommended in our *Standards for Internal Control in the Federal Government*.

To determine whether Energy's payments to contractors were properly supported and a valid use a government funds, we used a variety of data mining, document analysis, and other forensic auditing techniques to nonstatistically select transactions or groups of transactions for detailed review. For the transactions we selected, we reviewed supporting documentation to assess the appropriateness of payments based upon contract documents and applicable federal regulations, such as the *Federal Acquisition Regulation (FAR)*, *Federal Travel Regulation*, and *Joint Travel Regulations*. While we identified some payments as questionable or

improper, our work was not designed to identify all improper or questionable payments or to estimate their extent.

For each of the major contracts, we obtained copies of invoices from the contractor and compared the amounts to a listing of payments made by Energy. In addition to this high-level analysis, we performed detailed tests on labor and other direct costs, as described below.

Labor

We obtained an electronic file of all SEA labor charges, for both employees and subcontracted labor, for analysis. Based upon our review of the file for trends or anomalies, we nonstatistically selected 94 employees for testing. SEA provided personnel files containing supporting documentation, such as employee résumés, and company information, such as hire and termination dates. Because each person may have been billed under more than one labor category, we attempted to make 187 comparisons of personnel information to labor category requirements. SEA was unable to provide us with proper documentation of personnel obtained through temporary hiring agencies, thus preventing us from making 28 comparisons. We could not make an additional 72 comparisons because the contract's labor categories did not contain adequate education or experience requirements. We made 87 comparisons of employee qualifications to labor category requirements.

To review Westwood labor charges, we obtained compensation information, such as W-2s and 1099s, and compared certain amounts reported to underlying payment records and amounts Westwood billed the government for these costs. For 25 Westwood employees supporting OWA activities, we compared their education and experience requirements as documented on their résumés to the labor category requirements negotiated in its contract.

We also compared the documentation of the two TDI employees' qualifications to the contract labor category descriptions.

Other Direct Costs

Neither SEA nor Westwood provided a detailed list or breakdown of other direct costs as part of its invoice to Energy; therefore, we performed a preliminary review all the supporting documentation for these two contractors' other direct costs. From this documentation we identified a

high volume of the following types of transactions at each contractor, for which we performed a more detailed review.

- Payments for equipment and travel costs incurred by SEA. The supporting documentation we reviewed for these costs included expense vouchers, vendor invoices, travel authorization forms, and plane ticket receipts and itineraries.
- Payments for services provided by independent contractors incurred by Westwood. These services were mainly provided by the physician panel members. We obtained and reviewed the supporting invoices or other documentation of time and costs for 6 of 167 physician panel members billed. We chose these 6 physicians for detailed review because of the high volume of charges or unusual charges that we noted during our preliminary reviews of supporting documentation. We only considered their billings for fiscal year 2004, the year of the highest physician panel activity.

In addition to this review of payments made to the major contractors, we analyzed other payments made by Energy in support of OWA. For example, we requested supporting documentation for a nonstatistical selection of payments based upon our analysis of payment information by payee and amount. We also performed an analytical review of Department of Labor (DOL) reimbursements under memorandums of understanding dated July 2001 and December 2004 for the operation of the EEOICPA resource centers. These reimbursements totaled approximately \$11 million and were offset against costs for the Eagle contract and other OWA program activities.

We reviewed the November 29, 2005, settlement agreement and release between the Department of Justice and SEA resulting from investigations by the government of alleged improper billing by SEA. We also reviewed the related January 2006 administrative settlement agreement between the Department of the Navy and SEA that provided for SEA to implement a compliance program to ensure that it adheres to lawful and ethical procedures and practices in all areas relating to its role as a government contractor.

We provided Energy a draft of this report and SSC NOLA a draft of applicable sections of this report for review and comment. Energy's Deputy Assistant Secretary of Planning and Administration, Office of Environment, Safety and Health, and SSC NOLA's Commanding Officer provided written

comments, which are reprinted in appendixes II and III, respectively. Energy and SSC NOLA also provided technical comments, which we have incorporated as appropriate. We also provided key officials of SEA, Westwood, Eagle, and TDI with draft summaries of the findings noted in this report relating to them. We incorporated as appropriate oral and written comments we received on these draft summaries from management officials from Westwood, Eagle, and TDI and from outside legal counsel for SEA. We performed our work in accordance with generally accepted government auditing standards in Washington, D.C., and at three contractor locations from February 2005 through March 2006.

Comments from the Department of Energy

Note: GAO comments supplementing those in the report text appear at the end of this appendix.



Department of Energy

Washington, DC 20585

April 20, 2006

Linda M. Calbom
Director, Financial Management
and Assurance U.S. Government Accountability Office
441 G Street, NW
Room 5087
Washington, DC 20548

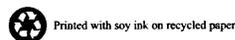
Dear Ms. Calbom:

Thank you for providing the Department of Energy (DOE) the opportunity to comment on the Government Accountability Office (GAO) review of internal controls for payments made to contractors and overall contract costs associated with DOE's implementation of the Energy Employees Occupational Illness Compensation Program Act of 2000 (EEOICPA). We have the following general comments:

- GAO provided 14 specific recommendations for DOE that have to do with improving controls over the review and approval of contractor invoices, strengthening accountability for Government owned equipment purchased by contractors, improving the reporting and control of overall contractor costs, and pursuing opportunities for recovery of any improper costs. DOE agrees with the spirit and intent of the recommendations. It should be noted that several recommendations have already been implemented and are addressed in the attached comments to the draft report. We will give careful consideration to each of the recommendations and will revise our current policies or procedures as appropriate.
- DOE has already undertaken a number of corrective actions, which are identified and discussed in the attached comments. However, many of the problems/issues identified by GAO were under the cognizance of the Department of the Navy (Navy) because they pertain to the Science and Engineering Associates (SEA) contract with the Navy. DOE obtained its primary contractual support from the Navy via an Economy Act Interagency Agreement under which the Navy utilized SEA as its support contractor through a Navy-SEA Blanket Purchase Agreement (BPA). The Navy assigned its own Project Manager to administer its BPA with SEA. DOE was a customer of the Navy and had no direct contractual relationship with SEA. DOE issued Acquisition Letter 2005-05 Rev on 4/26/05 addressing Interagency Contracting. The Acquisition Letter sets out new guidance and procedures that are stricter than the current requirements of the Economy Act and FAR 17.5. Moreover, specific guidance and training on the proper use of other agency contract vehicles was provided in December 2004, for all DOE contracting professionals and program officials. A DVD of this training was made and is posted on the Office of Procurement and Assistance Management's website for future reference by all DOE personnel and for training of new employees. Additionally, DOE has already initiated as standard operating procedure, audits through the Defense Contract Audit Agency (DCAA) of the contracts under DOE's cognizance that were

See comment 1.

See comment 1.



Appendix II
Comments from the Department of Energy

used in support of EEOICPA. We believe it is essential that this and other corrective actions taken by DOE be referenced in GAO's report.

As mentioned above, we have included as an attachment to this letter specific comments that would enhance the factual accuracy of your report. Due to the scope and extent of the comments, DOE respectfully requests that the entire text of this letter and its attachments be included in the published version of the GAO Report.

Sincerely,



Kevin Kelly
Deputy Assistant Secretary
Planning and Administration
Office of Environment, Safety and Health

Attachments: Detailed Comments on GAO-06-547
DOE Acquisition Letter 2005-05 Rev – Interagency Contracting

See comment 2.

Detailed Comments on GAO-06-547

GAO Comment: GAO implies that DOE did not ensure that the Government received good value from its Interagency Agreement with Navy and its contractor, SEA. (draft page 19 and elsewhere)

DOE Response: Energy did conduct observations and monitoring of SEA services, and linked those observations to the amounts SEA billed the Navy each month. Energy had multiple levels of metrics produced weekly that tracked cost, production, and quality. Energy received the contractor's cost report monthly and compared that to the number of contractor personnel and cases processed – Energy was constantly pushing for increased production and monitored these parameters closely. Based on the above, Energy was confident that it was receiving a good value for the Government's money.

GAO Comment: GAO reports that in June 2004, DOE transferred \$21.2 million to the program, while at the same time, legislation was moving through Congress to transfer the program, implying that DOE's ramp up activities were unsupportable. (draft page 10 and elsewhere):

DOE Response: DOE's reprogramming actions were proper.

- DOE properly reprogrammed \$21.2 million in June 2004 because Congress explicitly authorized it. DOE had presented its "ramp-up" plan to the Congressional committees, who approved the reprogramming action. The Congressional committees understood that DOE intended to use these funds to accelerate case production, and the committees approved the reprogramming and approved it.
- Agencies are required to act on the law as it stands, not on proposed legislation. Various legislative proposals to reform EEOICPA, including a proposal to transfer the program to another agency had been introduced previously and not been passed. The legislation proposed in June 2004 was substantially different from the bill ultimately passed in October 2004. DOE is not in a position to second-guess what proposed legislation may or may not become law and makes its reprogramming decisions based upon existing laws and existing programmatic need. DOE's reprogramming was proper, facilitated acceleration of case production and was approved by appropriate Congressional committees.

GAO Comment: GAO describes DOE actions in the procurement process (new contract to replace problematic Science and Engineering Associates, Inc. (SEA) and Westwood vehicles), stating that DOE had "substantially completed the procurement process by August 2004" but did not complete the action "in light of the potential transfer of the program to the Department of Labor." (draft page 14)

1

See comments 1 and 3.

See comment 1.

Appendix II
Comments from the Department of Energy

See comment 4.

DOE Response: The Contract Evaluation Team for the new contract did not provide its recommendations to the DOE Procurement Office until October 6, 2004 – more than a week after termination of the Navy’s SEA contract support. The proposed legislation to transfer the program to the Department of Labor (DOL) did not affect DOE’s decision making in August 2004. The DOE Bridge Contract was issued to allow for continuity of the program while the procurement action was finalized, and then served as the vehicle to close out the case processing activities.

GAO Comment: Although authority for contract oversight and administration was delegated among multiple agencies, ultimate responsibility for the contract rested with the customer agency (receiving agency), Energy. (draft page 16)

See comment 1.

DOE Response: We disagree with GAO’s assertion that the ultimate responsibility for the contract administration and oversight of the SEA contract rested with DOE as the receiving agency. The primary contractual support provided for the EEOICPA program was provided via an Economy Act Interagency Agreement with the Department of the Navy. The Navy elected to utilize SEA as its support contractor. The Navy had a competitively awarded Blanket Purchase Agreement (BPA) with SEA that was placed against a General Services Administration (GSA) Federal Supply Schedule contract. A GSA Contracting Officer, acting on behalf of the Navy placed the Agreement. Although DOE agrees that it has responsibility for its program, in this instance, we were a customer of the Department of the Navy. DOE had no direct contractual relationship with SEA, and the Navy had assigned its own Project Manager to administer the BPA. Issues regarding labor categories, rates and qualifications under the BPA were the direct responsibility of the Navy and the GSA Contracting Officer. GAO correctly notes that the Navy was responsible for the review and approval of SEA invoices and approval of contractor travel and contract deliverables.

See comment 1.

On November 29, 2005, the Department of Justice and SEA executed a Settlement Agreement and Release (Settlement) after an investigation of improper billings concerning labor charges by SEA under their GSA FSS contract and two related BPA’s. According to GAO, this included approximately \$26.6 million worth of support to the Department of Energy. Although both the Navy and GSA were clearly aware that there were serious issues with the SEA contract neither agency thought it necessary to advise DOE of these issues. In fact, it would appear that this investigation was going on at the same time DOE had requested the Navy to provide significantly increased staff support to the program. Under the terms of the Settlement, SEA paid the government \$9.5 million. In return the Government provided a release that it would seek no further civil or administrative monetary claims or cause of action against SEA. This would appear to preclude the recovery of any additional monies by the Navy/GSA for expenditures in support of DOE programs.

See comment 1.

Based on experience and lessons learned, DOE has already extensively revised its procedures for

Interagency Contracting. Some of the new requirements contained in the Acquisition Letter include: designation of a DOE Contracting Officer's Representative for Interagency Agreements and review by a DOE Contracting Officer when an existing servicing agency contract is utilized to ensure that proposed work is within the scope of the existing contract. These policies and procedures exceed the requirements in the Economy Act and its implementing regulations in FAR Subpart 17.5

GAO Comment: Labor categories and certain other activities were not verified against the contract. (draft pages 23 and 24):

See comment 1.

DOE Response: GAO notes that the Navy did not take proper steps to verify that labor hours were being billed at the appropriate rates and that employees were qualified under the labor category education and experience requirements negotiated in its BPA. They are asserting that DOE should have taken steps to ensure that the Navy implemented appropriate verification procedures or effective compensating control strategies. DOE disagrees with this assertion. The Navy and GSA (as its contracting representative) had complete cognizance of their BPA. However, as DOE had no privity of contract with SEA and was not involved in the placement or administration of the BPA, or any resulting task orders under the BPA, DOE was in no position to conduct any kind of independent verification of SEA's rates or personnel qualifications. We were relying on the service provider, in this instance GSA/Navy, to ensure that SEA complied with terms of its contract. We would note, however, that in light of the settlement that was reached by the Department of Justice with SEA, the Navy/GSA clearly recognized that there were issues with SEA labor rates and qualifications.

GAO Comment: Westwood performed some activities in support of the DOE Office of Worker Advocacy that were never incorporated into Westwood's Statement of Work. (draft page 24)

See comment 5.

DOE Response: DOE disagrees; the Statement of Work in the Westwood contract contains the following: "identifying and obtaining appropriate scientific, legal and medical expertise." This would include obtaining doctors (physician panels) and advisors on environmental health issues.

GAO Comment: Inadequate Consideration of Subcontractor Arrangements (draft pages 29 and 30):

See comment 1.

DOE Response: Again, DOE had no direct involvement in the negotiation or approval of subcontracting arrangements under the SEA contract. Those responsibilities lie directly with the service provider – the Navy/GSA. DOE would defer to the Navy/GSA to answer questions/concerns regarding SEA's subcontracting arrangements.

GAO Comment: With regard to the Technical Design, Inc. (TDI) contract, GAO is asserting that it was impossible for DOE to adequately review the amounts TDI billed for costs attributable to its subcontractor -- Westwood. (draft page 30)

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See comment 6.

DOE Response: DOE disagrees with this assertion. The TDI contract is an 8(a) contract that was issued on a cost-reimbursable basis. The contract was negotiated by DOE and a complete cost proposal for both TDI and its subcontractor Westwood was reviewed and approved by the DOE Contracting Officer at the time of award.

GAO Comment: GAO is indicating that an agreement (subcontract?) between TDI and Westwood does not exist. (draft page 30)

See comment 7.

DOE Response: While DOE agrees that TDI and Westwood should have entered into a subcontract, if for no other reason than their own protection, that issue has no bearing on whether or not the costs being billed were legitimate.

See comment 1.

The proper terms and conditions to ensure appropriate oversight and administrative controls were included in the TDI and Westwood contracts as they would be in any federal government contract. Accordingly, the Contracting Officer exercised his authority, pursuant to the terms and conditions of the contracts and initiated audits of the TDI and Westwood prime contracts and Westwood's subcontracts to ensure all billings are proper. This was done as part of the normal course of business and not as a result of GAO's audit. DOE would anticipate that many of the issues raised by GAO would have been identified in the normal course of auditing the contracts.

GAO Comment: GAO states that "physical inventories of Westwood and SEA purchased equipment were not completed until at least eight months following the expiration of the respective contracts." (draft page 28)

See comment 8.

DOE Response: This is incorrect. All SEA equipment was inventoried in the fall of 2004, during the closeout period, and DOE pursued charges for missing equipment. Westwood equipment was inventoried as well. All equipment was inventoried as it was placed on trucks for transportation from Forrester to Germantown. In Germantown, it was placed in temporary storage in 9 separate rooms. Compensation has been received from Westwood for some of the equipment and charges for other equipment are outstanding. We intend to recover any charges that are outstanding.

GAO Comment: Accountability for Equipment Purchased by Contractors was not maintained. DOE has identified 13 missing Westwood items. GAO has identified an additional 31 missing items, for a total of 44. (draft page 27-29):

See comment 9.

DOE Response: Of the list of 44 pieces of equipment that were identified as missing, after careful inventory review only 7 items remain missing. DOE has asked Westwood for reimbursement of the seven remaining items.

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Comments from the Department of Energy

There were issues with a lack of supporting documentation for Westwood purchases. DOE Office of Environment, Safety and Health (EH) has implemented the following *Corrective Action*: EH has instituted a pre-approval process for Other Direct Cost (ODC) items on contracts for any ODC in excess of \$50 (including travel).

GAO Comment: Contract Ceilings Were Not Effectively Monitored (draft pages 30 and 31):

DOE Response: GAO is asserting that there were numerous increases in contract ceilings for contracts supporting the OWA program. This is an accurate statement; however, the increases were necessitated by continually expanding program requirements. Each of the increases was reviewed and approved by both OWA and the DOE Contracting Officer and was properly effected in accordance with the FAR and internal DOE requirements. At no time did DOE exceed a contractually negotiated and established contract ceiling. The fact that modifications to the contract(s) were issued in a timely manner demonstrates that DOE was well aware of its ceilings and was managing them.

GAO Comment: Energy made millions of dollars in improper and questionable payments for contractor costs (draft page 32):

DOE Response: GAO is asserting that approximately \$26.4 million of improper or questionable payments were made to contractors supporting OWA activities. The bulk of this number - \$20,185,182 pertains to potentially "improper" and "questionable payments" regarding labor categories. It is the responsibility of the contractor to comply with the terms and conditions of its contract, including ensuring that the contractor's staff possesses the requisite minimum qualifications prescribed in the contract. As previously noted, the SEA contract (BPA) belonged to the Navy and it was their responsibility to ensure that the contractor complied with the terms of its contract. It was also the Navy's responsibility to conduct appropriate oversight and administration of contractor costs in accordance with the terms of the BPA, including any necessary audits. The Navy apparently recognized that there was an issue with some of SEA's personnel and initiated an investigation which resulted in a \$9.5 million settlement with SEA. Unfortunately, since neither the Navy nor GSA alerted DOE to the issues with its personnel, DOE was unable to proactively avoid the incurrence of questionable costs. In light of the settlement already reached with SEA it may no longer be possible to recover any additional overpayments.

In regard to the Westwood contracts, DOE is currently having the Defense Contract Audit Agency (DCAA) audit those contracts. These audits were initiated as part of DOE's normal course of business. Many of the issues that GAO is citing would normally be identified as part of a DCAA audit. After the audits are received, DOE will determine what action is warranted.

GAO Comment: GAO criticizes DOE for spending money on furniture and equipment in the summer of 2004. (draft page 33, and again more substantially on pages 46-47)

5

See comment 10.

See comment 1.

See comment 1.

DOE Response:

- DOE acted with Congressional approval of \$21.2 million in reprogrammed funds to accelerate its production activities, including providing furniture and equipment for its increasing staff. Had Congress not transferred the program, DOE would have been widely criticized for its failure to take timely steps to implement the plan submitted to Congress to accelerate production.

See comment 11.

- The furniture purchase is not an issue with contractual controls, which is the stated focus of this GAO report. There is nothing questionable (in terms of protocols, controls, or procedures) about the furniture purchase itself.

GAO Comment: GAO is asserting that both SEA and Westwood applied “mark-ups” in their fully burdened hourly rates for subcontracted labor, resulting in “improper” and “questionable” payments. GAO contends that the subcontracted labor should only have been billed at actual costs and that the hourly rates should not have contained “mark-ups.” (draft pages 39-42)

See comment 1.

DOE Response: Regarding GAO’s comments on the SEA contract we would defer to the Navy/GSA. With respect to the Westwood contract, DOE was billed at the fully-burdened rate of \$250/hr established in Westwood’s GSA FSS contract for the designated labor category for Senior Scientists. The rates contained in Westwood’s FSS contract were negotiated and approved by GSA and in accordance with the GSA Multiple-Award-Schedules (MAS) program which, in accordance with FAR subpart 8.4, are predetermined to be fair and reasonable. This rate was in fact the discounted rate from Westwood’s GSA schedule contract for that labor category. It is pertinent to note that, in its proposal to DOE, Westwood represented that the Senior Scientist positions were employees of Westwood and not independent contractors or subcontractors. DOE has initiated audits via DCAA of the Westwood contracts and these audits are currently being conducted. Any improper or questionable costs that are identified through those audits will be appropriately addressed by the Contracting Officer.

See comment 12.

With respect to GAO’s opinion and interpretation of the terms of FAR clause 52.232-7- Payments under Time-and-Materials and Labor-Hours contracts, it is relevant to note that the FAR Council published a proposed rule on September 26, 2005 (FAR Case 2004-015) to amend the clause, primarily to clarify the treatment of direct labor performed under Time-and-Material (T&M) contracts provided by subcontractors. Public comments were received in December 2005, and we understand the pending final rule will be issued shortly and that it will clarify that subcontract labor for other than incidental services be billed and paid at the contract fixed labor rate in accordance with the contract requirements applicable to the labor hour portion of the contract. This is consistent with our method established for T&M contracts requiring both primes and subcontractors to be reimbursed for direct labor based on their own established fully burdened labor rates.

See comment 1.

GAO Comment: GAO is criticizing DOE for paying add-on rates to Westwood that were “improper” and for overpaying the base fee to TDI and their subcontractor Westwood. (draft pages 43 and 44)

DOE Response: GAO is asserting that Westwood was improperly paid a 12% add-on rate for its Other Direct Costs (ODCs), which totaled \$557,429. DOE disagrees with this assertion. Westwood does have a currently approved rate of 13% for General and Administrative Expense (G&A) that is applied to its total cost base. This rate and its application base were verified by the Contracting Officer in a DCAA pre-award audit. We provided a copy of that pre-award DCAA audit to GAO previously along with the governing FAR policy. GAO’s objection appears to be that it was not specifically written into the task order. However, FAR 52.232-7- Payments under Time-and-Materials and Labor-Hours contracts, is applicable to Westwood’s task orders and this clause permits the application of an approved General and Administrative (G&A) rate to direct materials in accordance with the contractor’s usual accounting practices and FAR 31.2. However, the G&A rate and its application will be reviewed by DCAA in the course of conducting its audit(s) of Westwood’s task orders.

GAO is also asserting that Energy improperly paid \$98,305 in base fees to Technical Design, Inc. (TDI). DOE disagrees with this assertion. GAO is asserting that TDI exceeded both its base fee and the 10% limitation on fee at FAR 15.404. However, adding TDI’s fee to its subcontractor’s (Westwood’s) fee is not appropriate. While the TDI contract was a Cost-Plus-Award-Fee (CPAF) type, the subcontract with Westwood was a Cost-Plus-Fixed-Fee (CPFF) type. There is no “base fee” in Westwood’s CPFF subcontract. GAO is improperly adding the separate fees together to create one base fee pool. We would agree that neither TDI, nor its subcontractor (Westwood) was entitled to a fee in excess of 10% individually and DOE did not pay fee to TDI in excess of the 10% statutory limit.

GAO Comment: GAO is asserting that “improper” and “questionable” payments were made for Per Diem, Commuting and Travel Costs and that there were some duplicate and erroneous billings under the TDI and Westwood contracts. (draft pages 45 and 46)

See comment 1.

DOE Response: GAO is asserting that both SEA and Westwood over billed on per diem, commuting and travel costs. GAO also asserts that Westwood and TDI were overpaid due to duplicate and erroneous billings. Again, the SEA BPA would fall under the cognizance of the Navy/GSA. With regard to the Westwood contract, DOE is currently having DCAA audit all the prime and subcontracts. That would include any of the costs that GAO is questioning. After DOE receives those audits a determination of what, if any, action is required will be made. As previously mentioned, DOE’s Office of Environment, Safety and Health (EH) has implemented the following *Corrective Action*: EH has instituted a pre-approval process for Other Direct Cost (ODC) items on contracts for any ODC in excess of \$50 (including travel). This policy should eliminate over billings and erroneous billings on per diem, commuting and travel costs.

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Appendix II
Comments from the Department of Energy

See comment 13.

GAO Comment: GAO states that "by August 2004, OWA had initiated a hiring freeze in light of the potential transfer of the program to DOL." (draft page 47)

DOE Response: This statement is inaccurate. The legislation was not imminent in August 2004. The hiring freeze was to conserve funds in light of an expected (and extended) continuing resolution, which would have severely constrained the program's finances.

GAO Comment: GAO states that DOE did not seek a refund on the \$50,000 furniture assembly fee. (draft page 47)

See comment 14.

DOE Response: The systems furniture was used at 950 L'Enfant Plaza for swing space for the Forrestal Life Safety Sprinkler and Fire Alarm Installation Project. The \$50,000 of pre-paid installation charges from the manufacturer were used to install the systems furniture for that project. The installation took place from January 8, 2006 through February 13, 2006. DOE received full value for the installation dollars.

GAO Comment: Energy's monitoring of services provided under the Westwood contract was insufficient. (draft page 20)

See comment 15.

DOE Response: Although review and approval was done in the past, it was on a negative confirmation basis. DOE EH has implemented the following *Corrective Action*: DOE EH has since put in place positive confirmation approval on all EH invoices for support service contracts. Task Monitors (TM's) are required to sign off on the hours and other direct costs for each task under the contract. TM's are also required now to sign a memorandum explaining their responsibilities and duties as related to contract monitoring and other TM responsibilities.

GAO Comment: Energy did not request Westwood to submit supporting documentation for some ODCs because it was too voluminous. (draft page 24)

See comment 16.

DOE Response: It is not clear where the quote "too voluminous" came from. Regardless, DOE agrees that volume is not a reason to preclude submitting ODC documentation. DOE EH has implemented the following *Corrective Action*: DOE EH has established a new Other Direct Cost Policy, where all purchases in excess of \$50 must receive prior approval in writing by the Task Monitor (TM) and the Contracting Officer's Representative (COR) in order to receive reimbursement under the contract. The signed approval is to be submitted with the invoice as well.

GAO Comment: Energy improperly assigned some Westwood OWA costs to other program reporting units and, in some cases, assigned costs of other reporting units to OWA. (draft page 31)

Appendix II
Comments from the Department of Energy

See comment 17.

DOE Response: This only occurred for a short period. However, DOE EH has taken the following *Corrective Action*: Task Costs are billed to each office's B&R reporting code directly on each invoice. For cases where multiple offices use one task, specific delineation of employees and their specific costs are now received and used for billing to the correct B&R code.

GAO Comment: Energy "borrowed" \$1.3M from other program reporting units to pay OWA costs. (draft page 32)

See comment 4.

DOE Response: The \$1.3M from two other program reporting units was not "borrowed." It was transferred to OWA by senior DOE Management at the time. There was no plan to ever reimburse the offices providing the funding.

The following are GAO's comments on the Department of Energy's letter dated April 20, 2006.

GAO Comments

1. See the Agency Comments and Our Evaluation section.
2. We have not included the acquisition letter attached to this letter in this report. The letter can be found on Energy's Web site, www.doe.gov.
3. We did not assess or conclude on whether the government received "good value" from the contract with SEA. The scope of our work was to determine whether internal controls over program payments were adequately designed, and if program payments were properly supported as a valid use of government funds. We addressed financial management practices and procedures and whether payments were proper, not the value or quality of services received.
4. We modified the report for this additional information.
5. We disagree. Our report stated that the contract with Westwood did not fully reflect actual duties that were subsequently performed and provided three examples of such. The quotation provided by Energy in its comments is from the statement of work section of the Westwood contract entitled "Advisory Committee Activities" that only addresses the work that Westwood should perform in support of the Advisory Committee, and therefore this language does not address the other activities Westwood performed.
6. Energy states that a complete cost proposal was obtained from Westwood. However, Energy does not address that our report stated that Westwood's cost proposal was not incorporated into the prime contract with TDI nor was any other binding agreement created between Energy and Westwood relative to its cost proposal. Thus, as our report also stated, without an effective contractual agreement, including negotiated rates, it was not possible for Energy to adequately review the amounts TDI billed for costs attributed to what Energy characterizes as the subcontractor, Westwood. We reaffirm this position.
7. A formal agreement between a prime and a subcontractor not only protects the interests of the parties involved, but also those of the government. Additionally, as discussed in the Agency Comments and

our Evaluation section of our report, after-the-fact detective controls, such as the Defense Contract Audit Agency audits are not a replacement for real-time monitoring and oversight of contract costs.

8. At the time of our first inquiry, Energy told us it was still updating and finalizing the locations and conditions of the government-owned equipment that SEA purchased. On September 29, 2005, the Director of the Office of Information Management within the Office of Environment Safety and Health stated that “the identification and recording process is still underway.” This was 8 months after expiration of the SEA contract in December 2004. Our report also stated that an inventory of contractor-purchased, government owned equipment that Westwood purchased was not conducted until December 2005, nearly 9 months after Westwood’s contract expired, which Energy does not dispute.
9. We did not review Energy’s work in 2006 to address the missing items.
10. We do not agree with Energy’s statement that “at no time did Energy exceed a contractually negotiated and established contract ceiling.” Our report stated that Energy did not establish internal control monitoring practices to effectively manage overall contract costs, including using contract ceilings to manage and encourage cost-effectiveness. We found, for example, that Westwood was paid amounts that exceeded the “not to exceed” ceiling on other direct costs each year under its first contract, which covered the 3 ½ year period August 2001 through February 2005 as well as under the second contract that began in September 2004. As a specific example, the other direct cost ceiling was \$600,000 in year 3, but Westwood was paid \$2,421,176, or \$1,821,176 more than the “not to exceed” limit per the contract.
11. Our report stated that the scope of our work was to determine whether internal controls over program payments were adequately designed and if program payments were properly supported as a valid use of government funds. The furniture purchases were considered by us in the context of both objectives.
12. Our report recognized that there are different interpretations of the time and material payment clause (FAR 52.232-7). For purposes of our report, we have based our findings on the literal application of this clause. Further, as also stated in our report, we found that neither Energy nor SSC NOLA for SEA exercised sufficient management

oversight to be fully informed of the nature, extent, scope of services, and terms of billing to the government for subcontracted services. In addition, we found inconsistencies in the application of what Energy refers to in its comments as its “method established for T&M contracts of requiring both primes and subcontractors to be reimbursed for direct labor based on their own established fully burdened labor rates.”

13. Energy originally told us that the hiring freeze instituted in August 2004 was because of the combination of a probable continuing resolution and the possible transfer of the program to DOL. We modified the report based on Energy’s written comments.
14. We modified the report to reflect that the \$50,000 of up-front installation charges were paid in 2004 even though the equipment “was not installed until February 2006.” Notwithstanding this, the furniture installation fee, like the furniture, did not benefit OWA but rather another Energy program.
15. We did not review the procedures described as a corrective action to address our finding that Energy’s monitoring of services provided under the Westwood contract was insufficient. However, it will be important that changes are made to comprehensively address the conditions we found at the contractor and at Energy. Our report stated that the productivity measures used by the contractor to monitor work performed by physician panel members were developed based on the hours actually billed on the invoices submitted by the physicians, and therefore Energy had no independent baseline to measure productivity or to assess the reasonableness of hours billed on the invoices submitted by the physicians. Further, our report stated that doctors who performed a quality check function on claims were also not sufficiently monitored. Energy did not systematically observe the hours worked and compare any observations to the amounts paid for those hours, nor did it determine that Westwood was adequately monitoring these services as a basis for its billings.
16. The contracting officer’s representative told us that supporting documentation for Westwood’s invoices was not requested because of the “voluminous amounts” of paper that Westwood would need to copy and transmit to Energy each month. Our report stated that one of the elements of the control weakness for other direct costs was that the contractor was not required to report a detailed breakdown of its other direct costs as stipulated by its contracts. Without this level of

information, it was not possible for Energy officials to effectively review and approve these invoices for payment. Further, a substantial portion of the amount billed by Westwood for other direct costs was for temporary labor, and Energy's controls would not, therefore, be enhanced by the corrective action put in place covering purchases of \$50 or more. According to the implementation memo, this action is intended to address purchases such as government-owned equipment and travel, but does not specifically state whether temporary labor would be covered. It will be important for Energy to take further corrective actions that address enforcing its requirements for a detailed breakdown of other direct costs as well as controls specifically designed for temporary labor that are not covered by its new policy on purchases.

17. We disagree. Our report stated that Energy improperly assigned the costs of OWA services provided by Westwood to other program reporting units, in effect using other programs' funds to pay for OWA activities. We found that these practices occurred throughout the 4 years of the program for both the Westwood and TDI contracts, not just for "a short period" as Energy stated in its written comments.

Comments from the Space and Naval Warfare Systems Center, New Orleans



DEPARTMENT OF THE NAVY
COMMANDING OFFICER
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April 21, 2006

Linda M. Calbom
Director, Financial Management and Assurance
United States Government Accountability Office
441 G. Street, N.W.
Washington, D.C. 20548-0001

Dear Ms. Calbom:

Re: Space and Naval Warfare Systems Center, New Orleans, Response to
GAO Draft Report To Congressional Requesters, "Department of
Energy, Office of Worker Advocacy", April, 2006

Space and Naval Warfare Systems Center, New Orleans (SPAWARSYSCEN NEW
ORLEANS LA), appreciates the opportunity to provide comments to the
referenced Draft Report. Our responses are set forth below.

GAO Draft Report Recommendations for Space and Naval Warfare Systems
Center, New Orleans:

In light of the findings in this report, we recommend that the
Commanding Officer, Department of Navy's Space and Naval Warfare Systems
Center, New Orleans, reassess its procedures for carrying out its delegated
contract administration responsibilities, including the following:

-Assess the adequacy of the review and approval process for contractor
invoices, including (1) Oversight and monitoring of contractor services and
linkage of these activities to the invoice review and approval process,
(2) Verification that labor hours are billed in the appropriate categories at
the appropriate rates, and (3) Determining that contractor travel and other
direct costs are in accordance with the contract and applicable federal
regulations.

SPAWARSYSCEN NEW ORLEANS LA Response: Concur. The Commanding Officer will
ensure processes are in place to effectively accomplish the 3 recommendations
to improve the review and approval of contractor invoices. We will request a
review of our processes as a special interest item during the August 2006
triennial command inspection conducted by Space and Naval Warfare Systems
Command. Completion date: August 1, 2006

-Establish policies to document guidance sought from GSA and the
direction received on all matters of substance, including the use and billing
implications of subcontracted labor, and to communicate the direction
provided by GSA to the customer agency (e.g., Energy) for consideration by
the customer.

SPAWARSYSCEN NEW ORLEANS LA Response: Concur. Procedures for
documenting all significant communications and guidance from GSA or any
contract procurement or administrative source will be established. Training
for CORS and project/program managers will emphasize communication
documentation and effective sharing of information with customers and

Appendix III
Comments from the Space and Naval Warfare
Systems Center, New Orleans

stakeholders. This documentation will be required to be maintained as a part of the contract file. Completion date: August 1, 2006.

If you have questions or require additional information you may contact Mr. John Gampel, Acting Inspector General, Space and Naval Warfare Systems Command, who can be reached at (619) 524-7065 or John.Gampel@navy.mil.



FRED J. MINGO, JR.
Captain, U.S. Navy
Commanding Officer

Copy to:
SPAWAR Inspector General (Mr. John Gampel)

GAO Contact and Staff Acknowledgments

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Linda Calbom, (202) 512-9508 or calboml@gao.gov

Acknowledgments

In addition to the contact named above, staff members who made key contributions to this report include Robert Owens, Assistant Director; Marie Ahearn; Sharon O. Byrd; Richard Cambosos; Donald Campbell; Lisa Crye; Tyshawn Davis; Timothy DiNapoli; Abe Dymond; Ryan Geach; Jason Kelly; Dina Landoll; Patrick McCray; and Ruth S. Walk.

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